TAB D

frontier
A Citizens Communications Company

www.frontieronline.com

Regulatory Department
180 South Clinton Avenue
Rochester, NY 14646-0700

Tel: 585.777.5645
Fax: 585.262.5625
ken.mason@frontiercorp.com

VIA FCC ELECTRONIC COMMENT FILING SYSTEM

October 3, 2008

Ex Parte Presentation

Ms. Marlene Dortch
Office of the Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Re: High-Cost Universal Service Support; Federal-State Joint Board on Universal Service, WC Docket No. 07-267; CC Docket No. 96-45
Developing a Unified Carrier Compensation Regime, CC Docket No. 01-92

Dear Ms. Dortch:

In accordance with Section 1.1206 of the Commission's rules, 47 C.F.R. §1.1206, Frontier Communications Company provide notice of an ex parte meeting on September 29, 2008. Commission participants were Commissioner Michael Copps and Scott Deutchman, Competition and Universal Service Legal Advisor. Frontier participants were Maggie Wilderotter, Chairman, President and Chief Executive Officer, Kathleen Abernathy, Member of Frontier's Board of Directors, Dan McCarthy, Executive Vice President and Chief Operating Officer, and Ken Mason, Vice President – Government and Regulatory Affairs.

On the topic of Universal Service support, consistent with prior filings the Frontier participants suggested that the Commission can address a large a large part of the problem by requiring all recipients to have the same Carrier of Last Resort obligations, and by basing distributions on the recipients' individual costs. In addition, the Commission should evaluate under what parameters funding might be available for broadband investment to reach the most expensive customers to serve.

On the topic of intercarrier compensation, the Frontier participants urged the Commission to reject the reform proposals that suggest a $0.0007 terminating rate for all carriers. The revenue shifted out of intercarrier compensation would place a large burden on rural consumer rates as well as strain the Universal Service Fund (USF). Frontier would see the equivalent of $20.00 per month per customer displaced under a $0.0007 terminating rate in some of its most rural markets. Finally, if the Commission wants to provide immediate reform for intercarrier compensation in a short timeframe focusing on providing a Phantom Traffic solution and clarifying that IP originated traffic providers who utilize our networks should pay appropriate access charges would be positive first steps.

Respectfully submitted,

Kenneth Mason
Vice President – Government and Regulatory Affairs

TAB E

KELLEY DRYE & WARREN LLP
A LIMITED LIABILITY PARTNERSHIP
3050 K STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20007
(202) 342-8400

NEW YORK, NY
TYSONS CORNER, VA
CHICAGO, IL
STAMFORD, CT
PARSIPPANY, NJ

BRUSSELS, BELGIUM

AFFILIATE OFFICES
MUMBAI, INDIA

FACSIMILE
(202) 342-8451
www.kelleydrye.com

DIRECT LINE: (202) 342-8531
EMAIL: gmorelli@kelleydrye.com

October 3, 2008

VIA ECFS

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th St., SW
Washington, D.C. 20554

Re: *Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92

Dear Ms. Dortch:

Recently, renewed attention has been directed to the question of whether bill-and-keep is an appropriate approach to intercarrier compensation reform. On September 24, 2008, Qwest Corporation ("Qwest") filed an ex parte letter urging the Commission to adopt bill and keep as the "ideal solution for comprehensive ICC reform."[1] We have been asked to respond to Qwest submission on behalf of Cavalier Telephone, Nuvox, and XO Communications.

In Qwest's view, a bill-and-keep approach to intercarrier compensation, rather than a system where carriers pay regulated rates to each other for transport and termination, is "the only solution that is a comprehensive fix of all of the broad variety of arbitrage problems … that underlie the current ICC regime."[2] The Commission should reject Qwest's suggestion for the reasons explained below. Before the Commission even considers Qwest's appeal, however, it should ensure that its record on bill-and-keep is up-to-date and that all interested parties have

1 Letter from Melissa E. Newman, Vice President, Qwest, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, WC Docket No. 05-337, CC Docket No. 96-45, CC Docket No. 99-68, WC Docket No. 07-135 and WC Docket No. 04-36 (filed Sept. 24, 2008) ("*Qwest Sept. 24th Ex Parte*"), at 2.

2 *Id.*, at 8.

been afforded the opportunity to express their views by providing an additional round of comment on this issue.

I. THE RECORD REGARDING BILL-AND-KEEP IS STALE

Qwest's submission attempts to reverse prior Commission orders rejecting mandatory bill-and-keep, and revive a debate that has been dormant at the Commission for several years. In 2000, an OPP Working Paper by Patrick DeGraba proposed a unified approach to interconnection pricing called Central Office Bill and Keep.[3] That proposal generated considerable discussion and disagreement that carried through to the Commission's 2005 *Further Notice of Proposed Rulemaking* ("*FNPRM*") in this docket.[4] Since that time, however, various comprehensive intercarrier compensation proposals, all of which include ongoing charges for traffic termination, – including the Missoula Plan[5] and, more recently, the Verizon plan[6] – have been offered and debated extensively on the record. At the same time, there has been virtually no discussion or advocacy regarding mandatory bill-and-keep and the record regarding bill-and-keep has become hopelessly stale. For that reason, the Commission should not even consider adopting a mandatory bill-and-keep scheme without first seeking additional input from interested parties through a new round of comments. Further, because the adoption of a mandatory bill-and-keep regime would represent a radical departure from the alternatives that have been under active consideration at the Commission for the past several years, the Commission must provide an additional opportunity to comment on the approach in order to ensure that interested parties' due process rights are protected.

II. THE COMMISSION CANNOT LAWFULLY COMPEL INDUSTRY-WIDE BILL AND KEEP ARRANGEMENTS

As is demonstrated hereinafter, the adoption of mandatory bill-and-keep arrangements is extremely ill advised as a policy matter. Apart from the theoretical merits of a bill-and-keep system, however, it is critical to understand that the Commission simply lacks legal

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3 DeGraba, Patrick, *Bill-and-Keep at a Central Office as the Efficient Interconnection Regime*, OPP Working Paper No. 33 (Dec. 2000) ("*DeGraba Paper*"), at ¶ 4

4 *Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, *Further Notice of Proposed Rulemaking*, FCC 05-33 (rel. Mar. 3, 2005) ("*Intercarrier FNPRM*").

5 *Ex parte* letter from the NARUC Task Force on Intercarrier Compensation to FCC Chairman Kevin J. Martin, CC Docket No. 01-92 (Jul. 24, 2006), including attachments containing the Missoula Plan, the Executive Summary of the Missoula Plan, and a Legal and Policy Overview of the Missoula Plan.

6 Letter from Susanne A. Guyer, Senior Vice President, Verizon, to Chairman Kevin Martin, Federal Communications Commission, CC Docket No. 01-92, CC Docket No. 96-45 (filed Sept. 12, 2008).

authority to require all local exchange carriers ("LECs") to exchange traffic on a bill and keep basis. Congress was clear in adopting Section 251(b)(5) the 1996 Act that the touchstone for establishing rates for interconnection is "cost", and that all LECs are entitled to charge rates that recover their just and reasonable costs of providing interconnection services. The specific rate to be charged is not specified, but it is eminently clear that "free" is not a result that the Commission can impose.

The legal roadmap for establishing pricing for interconnection services provided pursuant to Section 251(b)(5) is found in Section 252(d). Congress specified therein that pricing for reciprocal compensation is "just and reasonable" only when the rates allow for the "mutual and reciprocal recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier." [7] Clearly, LECs have a statutory right to recover the costs incurred in terminating traffic for other carriers. Critically, it is equally clear under the statute that LECs have a right to recover those costs by charging the carrier that delivers traffic for termination. "Mutual" means "common to both parties...each acting in return or correspondence to the other...", and "reciprocal" is defined as "directed by each other toward the others...."[8] Accordingly, the statute is express that LECs are to recover the cost of terminating traffic by charging each other, and not by shifting the burden to third parties, such as by increases in end user subscriber line charges ("SLCs") or through some new governmental universal service mechanism such as the Recovery Mechanism ("RM") proposed by Verizon. The Commission is thus statutorily barred from requiring all LECs to implement bill and keep arrangements.

Of course, the Act does not preclude individual LECs from voluntarily negotiating agreements that incorporate bill and keep arrangements. Sec. 252(d)(2)(B)(i) permits LECs to "waive" their rights to mutual recovery when they determine that there is an "offsetting of reciprocal obligations." In other words, when LECs determine that the exchange of traffic is in balance, they can voluntarily agree between themselves to exchange traffic on a bill-and-keep basis. But the notion of waiver necessarily means a knowing and voluntary relinquishment of rights. Regulators cannot make that judgment for them; certainly at least not without examining whether the exchange of traffic between two discrete carriers are highly likely to be in balance. Neither the FCC or state commissions can make an industry-wide assessment of whether traffic is likely to be in balance, and cannot compel LECs to waive their rights to reciprocal compensation that recovers the "additional costs of terminating such calls."[9]

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7 47 U.S.C. § 252(d)(2)(A)(i)

8 Black's Law Dictionary, 7th Ed. Pp. 707, 1276.

9 47 U.S.C. § 252(d)(2)(A)(ii)

Importantly, the Commission already has determined that bill and keep arrangements do not provide for recovery of costs as required by the Act. In its seminal *Local Competition Order*, the Commission examined this issue and found that "carriers incur costs in terminating traffic that are not de minimis and, consequently, bill and keep arrangements that lack any provisions for compensation do not provide for recovery of costs."[10] The Commission went on to observe that "as long as the cost of terminating traffic is positive, bill and keep arrangements are not economically efficient because they distort carriers' incentives, encouraging them to overuse competing carriers' termination facilities by seeking customers that primarily originate traffic," and observed that when traffic is in fact likely to be in balance, it is reasonable to believe that LECs would exercise their statutory right to enter into bill-and-keep arrangements voluntarily.[11] The Commission did not bar state commissions from imposing bill and keep arrangements in discrete situations, but made clear that states could require bill-and-keep only where they determined after investigation of particular carriers that the "traffic is roughly balanced in the two directions and neither carrier has rebutted the presumption of symmetrical rates."[12]

Thus, apart from the policy shortfalls of Qwest's proposal, it is clear that the Commission cannot implement it without first seeking statutory changes from Congress.

III. MANDATING BILL-AND-KEEP WOULD REQUIRE A MASSIVE RATE INCREASE TO END USERS

Intercarrier compensation charges today are used to recover the massive investment that both ILECs and CLECs have made in their networks, including investment to deploy broadband facilities to an ever-expanding number of customers. As both the Verizon and AT&T plans for intercarrier compensation reform recognize, any reduction in intercarrier compensation revenue must be recovered elsewhere, and that "elsewhere" is from end users in the form of increased SLCs and USF charges (*i.e.* the so-called RM). What Qwest ignores is that adopting a universal bill-and-keep system -- and effectively setting an access charge and reciprocal compensation rate of zero -- would result in massive rate shock to enormous numbers of consumers of telecommunications services.

While we do not have access to AT&T's cost model -- and note that AT&T has every incentive to understate the impact of such shifts in cost recovery responsibility -- we

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10 In the Matter of Implementation of the Local Competition Provisions n the Telecommunications Act of 1996, First Report and Order, 11 FCC Rcd 15499. ¶112 (Rel. Aug. 8, 1996).

11 Id.

12 Id.

observe that they recently estimated that setting a unified terminating rate of zero would require a total access recovery shift from carriers to end users of $4.3 billion.[13] Coupled with the AT&T/Verizon proposal to switch to a telephone number based system of USF assessment, this massive shift in cost recovery would result in an unprecedented rate shock to end users, particularly low and moderate volume users of telecommunications services. We note that there is no requirement that interexchange carriers be required to pass-through the windfall realized from receiving free call termination services, and it is unrealistic to think that they will do so.

Such an enormous spike in end user charges simply is unnecessary to solve the arbitrage problems with which the Commission is concerned. There has been no showing that arbitrage would present a significant problem if current reciprocal compensation rates were used as a basis to establish a unified terminating intercarrier compensation rate. Yet use of existing reciprocal compensation rates instead of bill-and-keep would greatly reduce the adverse impact on end users. While we are unable to calculate the specific revenue recovery shift to end users, it appears that use of average current reciprocal compensation rates (rather than bill-and-keep) would reduce the adverse impact of intercarrier compensation reform to end users by more than 75 percent, while still solving any existing significant access arbitrage problems.

IV. MANDATORY BILL-AND-KEEP WOULD SEND INAPPROPRIATE MARKET SIGNALS THAT WOULD RESULT IN SIGNIFICANT MARKET DISTORTIONS

Qwest is incorrect that mandatory bill-and-keep is "the only solution that is a comprehensive fix of all of the broad variety of arbitrage problems"[14] of the current intercarrier compensation system. In reality, a mandatory bill-and-keep regime would send inappropriate economic signals that would result in market distortions not unlike those being experienced today. Instead, the Commission should adopt a cost-based terminating compensation rate while continuing to make bill-and-keep available for use by carriers on a voluntary basis. If compensation rates are cost-based, there will be a natural incentive for carriers to enter into bill-and-keep arrangements when traffic is in balance.

Qwest and other bill-and-keep proponents fail to note that longstanding industry pricing practices that govern the majority of interconnection arrangements for voice traffic already provide for a balance regime of "calling party's network pays" ("CPNP"), whereby the calling party's network pays the called party's local network to terminate a call, and "called party

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13 *See*, AT&T Ex Parte filing, "The Path to a Broadband Future -- Unified Terminating Rates," CC Docket No. 01-92 filed Sept. 12, 2008.

14 *Qwest Sept. 24th Ex Parte*, at 8.

pays", through the imposition of subscriber line charges.[15] This balanced regime is based on the Commission's experience in weighing the benefits of the call to the calling and called parties. Qwest and the other advocates now seek to have the Commission adopt a new threshold premise that of a bill-and-keep regime, whereby it is assumed that the benefits of all calls are shared equally by the calling and called parties.[16] Thus, bill-and-keep proponents argue that calling and called parties should each bear their own costs – a result that assigns the costs of origination to the calling party and the costs of termination to the call recipient.[17] However, while supporters of bill-and-keep characterize CPNP regimes as based on "outdated and faulty assumptions that only calling party end users benefit from a given call,"[18] they do not offer any support for the proposition that calling and called parties benefit equally (and are equally willing to share the costs). Without such evidence, the Commission can only proceed on blind-faith, a completely unacceptable justification for action that will substantially affect so many consumers and telecommunications providers.

Bill-and-keep proponents attempt to back into the conclusion that calling and called parties benefit equally by pointing out that there are various mechanisms that permit consumers to avoid incoming calls.[19] Proponents argue that by actively choosing not to receive some incoming calls (through blocking, screening, or simply not answering), end users demonstrate that calls not avoided must be beneficial. Such conjecture – without substantive support – is not a legitimate basis for overturning longstanding pricing relationships based upon CPNP. Indeed, in reality, it is simply not possible to quantify the benefits received by calling and called parties with enough precision to provide a reasoned basis for intercarrier compensation relationships.[20] At the same time, the following facts are indisputable: (1) the calling party affirmatively selects the person to be called and the time at which the call is placed; (2) the calling party knows who is being called, the nature and purpose of the call, and how much

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15 In the case of a local call, the calling party's LEC is required to pay transport and termination for traffic that terminates on the called party's network. In the case of a long-distance call, the calling party's interexchange carrier pays terminating access charges, either interstate or intrastate, to the called party's LEC to terminate the call and originating access charges to the calling party's LEC to originate the call.

16 *See, e.g., DeGraba Paper* at ¶ 4; *Qwest Sept. 24th Ex Parte*, at 9.

17 It bears noting that even under a CPNP system calls are not cost-free to called parties. The called party incurs costs associated with receiving calls by maintaining an access line and choosing to permit that access line to be occupied for the duration of a particular call.

18 *Qwest Sept. 24th Ex Parte*, at 9.

19 *See, e.g., Intercarrier FNPRM*, at ¶ 31.

20 For example, a call that might be considered beneficial to the called party at 1:00 p.m. might not be considered beneficial if received at 1:00 a.m. and certain calls (*e.g.*, calls from telemarketers or fundraisers) may never be considered beneficial to the called party.

the call will cost; (3) not every call attempt is answered by the called party;[21] and (4) end users can voluntarily agree to pay for incoming calls through subscription to 800-type services. These facts illustrate why it is entirely reasonable to continue to require that the calling party bear the costs of completing a call.[22]

Bill-and-keep proponents are quick to point to "the arbitrage problems that plague the current regime,"[23] blaming those problems on the "vastly disparate rates applicable to services that are functionally identical."[24] Yet advocates of bill-and-keep fail to acknowledge that the regulatory arbitrage they criticize as an unacceptable byproduct of the current intercarrier compensation system would persist in different form under a bill-and-keep regime, particularly the type of regime advocated by Qwest where originating charges are omitted from the plan. Arbitrage opportunities occur when carriers are able to "revise or rearrange transactions to exploit a more advantageous regulatory treatment, even though such actions, in the absence of regulation, would be viewed as costly or inefficient."[25] Arbitrage opportunities exist under the current CPNP system in part because carriers have the ability to shift costs to competitors (*i.e.*, originating carriers) by seeking customers with high *inbound* calling patterns. Under a bill-and-keep system, however, regulatory arbitrage would persist, except in the opposite direction. Carriers would seek out customers with high *outbound* calling requirements, offering them prices that reflect the fact that they would not be required to pay to terminate those outbound calls. As noted by Verizon in response to the *FNPRM*, "the default bill-and-keep rule proposed by some would encourage a whole new set of arbitrage opportunities."[26]

This arbitrage potential is heightened by the consolidation among the largest incumbent local exchange carriers ("ILECs") – the Regional Bell Operating Companies (RBOCs") – that has occurred over the past several years. As the RBOCs' incumbent operating

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21 In a busy or no answer situation, the called party receives zero benefit but the calling party receives the positive benefit of knowing the called party is not available.

22 Moreover, as Verizon has pointed out, if the Commission mandates a bill-and-keep regime, "[it] will therefore be required to defend … the plainly erroneous premise that interconnection always provides roughly equivalent benefits to the interconnecting carriers – under the same standards that would apply were it to choose any positive rate." Comments of Verizon in Response to FNPRM, CC Docket No. 01-92 (filed May 23, 2005) ("*Verizon Comments*"), at 23 (footnote omitted).

23 *Qwest Sept. 24th Ex Parte*, at 2.

24 *Id.*, at 5.

25 *Intercarrier FNPRM, Appendix C: A Bill-and-Keep Approach to Intercarrier Compensation Reform, An Analysis of Pleadings in CC Docket No. 01-92 by the Staff of the Wireline Competition Bureau* ("*Staff Report*"), at 102.

26 *Verizon Comments*, at 4.

territories expand, a growing percentage of calls are completed entirely within the RBOC's network. Thus, the overwhelming number of local calls and a very sizable percentage of long distance calls no longer involve any intercarrier payments. Yet the RBOCs have not adjusted their retail pricing to reflect the fact that they are no longer being required to make intercarrier compensation payments to terminate calls. At the same time, very few, if any, of the calls handled by a small competitive local exchange carrier ("CLEC") or interexchange carrier ("IXC") are originated, transported, and terminated entirely on that carrier's own facilities. Since smaller carriers would not be able to raise their rates to end users to recover foregone intercarrier compensation revenue should the Commission mandate a bill-and-keep regime, smaller carriers would be placed at a significant competitive disadvantage relative to the RBOCs under mandatory bill-and-keep. Thus, competitive neutrality considerations dictate that smaller carriers continue to be afforded the opportunity to obtain compensation for the termination of calls originated on other carriers' networks through intercarrier compensation arrangements.

Competitive neutrality concerns also arise due to the fact that mandatory bill-and-keep arrangements are not designed to accommodate non facilities-based carriers. The underlying presumption of bill-and-keep is that market equilibrium will result from the exchange of traffic by fully-functional facilities-based networks. In reality, however, not all carriers have facilities-based networks. The market contains various specialized non facilities-based service providers. As explained by BellSouth in comments in response to the *FNPRM*, mandatory bill-and-keep is not competitively neutral because it fails to provide a facilities-based carrier with the ability to capture any portion of the value its network creates for a non facilities-based provider:

> [A]ssume there are three carriers: Carrier A, an interexchange carrier, Carrier B, a full service (local and interexchange) carrier and Carrier C, a local carrier. Assume that a call between end users served by Carrier B and Carrier C is an interexchange call. If Carrier A and Carrier B compete in the interexchange market segment, under a bill-and-keep arrangement, both carriers would have to bear the cost of interexchange transport, but only Carrier B has to bear the cost of the local network where the call originates. The result is not competitively neutral.[27]

In addition, mandatory bill-and-keep provides disincentives for network investment:

> Furthermore, such a result would distort economic entry by denying the local carrier, Carrier C, the opportunity to recover the cost of enabling the interexchange call. Consequently, because

27 Comments of BellSouth Corporation, CC Docket No. 01-92 (filed May 23, 2005) ("*BellSouth Comments*"), at 10.

> Carrier C will not be able to capture even a portion of the value its network creates for Carrier B and its customers, Carrier C's investment in its network will be inefficiently distorted.

In short, a mandatory bill-and-keep system would provide disincentives for investment in networks and network improvements, as network owners would be unable to recoup the value created by those investments. At the same time, other providers would have strong incentives to free ride on the investments of facilities-based service providers. The disincentive to network investment created by mandatory bill-and-keep is directly at odds with the Commission's longstanding and oft-stated policy goal to promote network facilities deployment and facilities-based competition.[28]

Finally, the lack of competitive neutrality in the bill and keep regime proposed by Qwest is further evidenced by its declaration that the regime must include several additional policies: new local interconnection requirements, a new access recovery mechanism to make incumbent local exchange carriers whole, and the ability for incumbent to impose selectively subscriber line charges. Each of these proposals is blatantly biased in favor of incumbent carriers and will inhibit competition. In addition, each is legally suspect. They provide additional justification that a bill and keep regime may have superficial appeal at first glance but lacks real benefits when subjected to close scrutiny.

V. CONCLUSION

A regime that limits compensation to forward-looking economic costs is the only real means to eliminate arbitrage and to ensure continued network investment. The Commission should reject Qwest's call for mandatory bill-and-keep and should instead expeditiously adopt a cost-based rate for termination of all traffic within the federal jurisdiction.

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28 Furthermore, under mandatory bill-and-keep, the terminating carrier has less incentive to provide good service since it is not getting paid for the termination service it provides.

Sincerely,

Brad E. Mutschelknaus
Genevieve Morelli
KELLEY DRYE & WARREN LLP
Washington Harbour
3050 K Street, N.W., Suite 400
Washington, D.C. 20007
202-342-8539 (phone)
202-342-8451 (facsimile)
bmutschelknaus@kelleydrye.com

cc: Nicholas G. Alexander
Amy Bender
Scott Bergmann
Scott M. Deutchman
Greg Orlando
Dana Shaffer
Don Stockdale
Jennifer McKee
Marcus Maher
Jane Jackson
Al Lewis
Bill Sharkey
Jay Atkinson
Doug Slotten
Claude Aiken
Nicholas Degani
Victoria Goldberg
Lynne Engledow
Alex Minard
Matt Warner
Tom Buckley
Greg Guice
Rebekah Goodheart
Randy Clarke

Matthew Berry
Ajit Pai
Christopher Killion
Paula Silberthou

TAB F

NECA 25 YEARS OF Excellence
80 South Jefferson Road
Whippany, NJ 07981

Richard A. Askoff
Executive Director - Regulatory
PH 973 884-8350
FX 973 599-6636
raskoff@neca.org

October 6, 2008

Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Re: Developing a Unified Intercarrier Compensation Regime
CC Docket No. 01-92

Dear Ms. Dortch:

In recent weeks various parties have submitted *ex parte* letters suggesting the Commission overhaul existing intercarrier compensation mechanisms by establishing uniform compensation rules that would limit per-minute termination charges for all carriers to $0.0007 per minute.[1] These proposals raise significant concerns among NECA pool members, who depend on cost-based access charges to continue providing high-quality service to customers in rural areas.[2]

Proponents of such concepts have not explained how a uniform rate structure would be implemented, nor (until recently) have they explained what legal rationale the Commission might use to impose a uniform rate on all intercarrier compensation traffic.[3] On September 19, however, Verizon filed a memorandum asserting that changes in technology and the marketplace (primarily, growth in wireless and IP-enabled services) make it increasingly difficult for carriers to determine the beginning and endpoint of calls, and these circumstances now warrant federal preemption of all intercarrier compensation mechanisms.[4] Preemption, according to Verizon, would enable the Commission to use its ratesetting authority under sections 201 and 332 of the Act to reform intercarrier compensation nationwide, by prescribing a single, federal default termination rate of $0.0007 per minute to all intercarrier traffic.

Like Verizon, rural rate-of-return companies increasingly find themselves embroiled in complicated and expensive disputes over which rates apply to traffic terminating on their networks.[5] NECA has expressed

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[1] Letter from Susanne A. Guyer, Verizon, to Chairman Martin and Commissioners Copps, Adelstein, Tate, and McDowell, CC Docket No. 01-92 (Sept. 12, 2008) (*Verizon Proposal*); Letter from AT&T, Verizon, The VON Coalition, *et al.*, to Chairman Martin and Commissioners Copps, Adelstein, Tate, and McDowell, WC Docket No. 04-36, CC Docket No. 01-92 (Aug. 6, 2008) (*Coalition Proposal*).

[2] *See e.g.*, Letter from Ken Pfister, Great Plains Communications, to Marlene H. Dortch, FCC, CC Docket Nos. 01-92, 99-68 (Sept. 17, 2008); Letter from Tom Karalis, Fred Williamson & Associates, to Marlene H. Dortch, FCC, CC Docket No. 01-92 (Sept. 26, 2008) (on behalf of the Rural Alliance, *et al.*) (*Rural Alliance*); Letter from Daniel Mitchell, NTCA, to Marlene H. Dortch, FCC, CC Docket No. 01-92, WC Docket No. 04-36 (Sept. 12, 2008).

[3] *See e.g.*, Letter from Kathleen O'Brien Ham, T-Mobile, to Marlene H. Dortch, FCC, WC Docket No. 04-36 (Aug. 27, 2008); Letter from Norina Moy, Sprint Nextel, to Marlene H. Dortch, FCC, CC Docket No. 01-92 (Sept. 19, 2008).

[4] *See* Letter from Donna Epps, Verizon, to Marlene H. Dortch, FCC, CC Docket No. 01-92 (Sept. 19, 2008), attaching White Paper (*Verizon*).

[5] *See e.g.*, Letter from Joe A. Douglas, NECA, to Marlene H. Dortch, FCC, WC Docket No. 04-36, CC Docket No. 01-92 (May 23, 2008); Letter from Joe A. Douglas, NECA, to Kevin J. Martin, Chairman, FCC, CC Docket No. Docket No. 01-92

strong support for intercarrier compensation reform that would help resolve these problems. For example, by confirming access charges apply to interconnected VoIP traffic, as NECA and numerous other parties have repeatedly suggested,[6] the Commission could resolve many of the problems identified by Verizon with respect to IP-enabled traffic.[7] Similarly, the Commission has received several proposals suggesting reasonable means for determining the jurisdiction of wireless calls and for dealing with various forms of phantom traffic.[8] Verizon and other wireless carriers have steadfastly opposed these measures, however.[9]

In any event, there is no basis for imposing a single *uniform* rate on all carriers.[10] Verizon asserts in this regard there is "no reason to believe" multiple, reasonable approximations of the additional costs of terminating § 251(b)(5) traffic exist.[11] But costs of transport and termination do vary widely among carriers. In fact, for most rural companies a $0.0007 rate would not be sufficient even to cover costs incurred to bill minutes of use.[12] And, while Verizon and other carriers may have entered into agreements establishing rates at or below $0.0007 per minute, this hardly constitutes "substantial evidence" $0.0007 per minute is just and reasonable for all.[13]

(Nov. 13, 2007); Letters from Joe. A. Douglas, NECA, to Marlene H. Dortch, FCC, CC Docket No. Docket No. 01-92 (Oct. 16, 2007 and May 2, 2007).

[6] *Id. See also*, Letter from Stuart Polikoff, OPASTCO, to Marlene H. Dortch, FCC, WC Docket Nos. 05-337, 06-122, 04-36 and CC Docket Nos. 96-45 and 01-92 (Sept. 16, 2008); Letter from Daniel Mitchell, NTCA, to Marlene H. Dortch, FCC, CC Docket No. 01-92 and WC Docket No. 04-36. (Sept. 30, 2008); Letter from Curt Stamp, ITTA, to Marlene H. Dortch, FCC, CC Docket No. 01-92 and WC Docket No. 04-36 (Aug. 14, 1008).

[7] Verizon describes at length problems associated with identifying the origination and termination points of "calls" made using various IP-enabled technology. *See. e.g., Verizon* at 15. But these issues are not applicable to calls made using "fixed" VoIP services, *See. e.g.* Letter from James Bradford Ramsay, NARUC, to Chairman Martin, FCC, CC Docket No. 08-152 (Aug. 26, 2008).

[8] *See e.g.*, NECA Petition for Interim Order, CC Docket No. 01-92 (Jan. 22, 2008); Letter from Joe A. Douglas, NECA, to Marlene H. Dortch, FCC, CC Docket No. 01-92 (Apr. 24, 2008) (proposing extension of call signaling rules to interconnected VoIP providers, and use of originating and terminating telephone numbers to jurisdictionalize traffic in the absence of location-specific information or reasonable negotiated factors).

[9] *See e.g.*, Verizon Comments, CC Docket No. 01-92 (Dec. 7, 2006); Letter from Paul Garnett, CTIA, to Marlene H. Dortch, FCC, CC Docket No. 01-92 (Feb. 25, 2008), at 3.

[10] *See e.g.*, Letter from Daniel Mitchell, NTCA, to Marlene H. Dortch, FCC, CC Docket No. 01-92 (Sept. 30, 2008); Letter from Anne C. Boyle, Nebraska PSC, to Chairman Martin, FCC, CC Docket No. 01-92 (Sept. 30, 2008); Letter from David Bergmann, NASUCA, to Chairman Martin, FCC, CC Docket No. 01-92 (Sept. 30, 2008), at 2-3; Letter from Jonathan Lechter, Willkie Farr & Gallagher LLP (on behalf of Time Warner and One Comm.), to Marlene H. Dortch, FCC, CC Docket No. 01-92 (Oct. 2, 2008), presentation at 2-4.

[11] *Verizon* at 27.

[12] NECA analyzes carrier access billing system (CABS) cost data reported by small cost companies as part of its annual average schedule study, conducted pursuant to section 69.606 of the Commission's rules. NECA's most recent study showed interstate CABS billing costs for small cost companies of $0.001706 per minute -- nearly 2.5 times higher than the proposed $0.0007 rate. *See* NECA 2008 Modification of Average Schedules, WC Docket No. 07-290 (Dec. 21, 2007) at VII-12 *et seq.*

[13] A $0.0007 rate may well be reasonable for large integrated carriers such as Verizon or AT&T. But rural rate-of-return carriers receiving traffic via indirect interconnection arrangements lack negotiating leverage, and often find themselves forced to agree to below-cost reciprocal compensation rates in "take it or leave it" negotiations with wireless carriers and other larger providers. *E.g.*, Letter from Joe A. Douglas, NECA, to Marlene H. Dortch, FCC, CC Docket No. 01-92 (Apr. 24, 2008), presentation at 6-8. Agreements arrived at in this manner hardly constitute evidence a $0.0007 rate is just and reasonable for all carriers.

Verizon also claims section 252(d)(2) of the Act "expressly precludes" regulators from engaging in carrier-specific analysis of the costs of terminating traffic.[14] But that section of the Act, read in context, clearly contemplates examination of individual carrier costs in determining prices for transport and termination.[15] It certainly does not mandate a single nationwide rate, particularly one that is below incremental cost levels incurred by rate-of-return carriers in providing service in rural areas.[16]

Prescription of a nationwide uniform default rate of $0.0007 is unnecessary to solve the rate arbitrage problems identified by Verizon. It would also represent bad policy.[17] Such below-cost rates would likely encourage new forms of uneconomic arbitrage, as well as abuse of the network.[18] Moreover, transferring a disproportionate share of network costs caused by interconnecting carriers to alternative recovery mechanisms runs the risk of unduly burdening the universal service fund.[19]

A more reasonable approach would be to permit, not require, carriers to set unified originating and terminating access rates. Such rates must (a) recognize differences in costs and operational circumstances among carriers or groups of carriers and (b) maintain a reasonable balance of network cost recovery among intercarrier compensation charges, end user rates and universal service funding.[20]

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[14] *Verizon* at 27.

[15] *See, e.g.*, 47 U.S.C. § 252(d)(2)(A)(i) (rates must "provide for the mutual and reciprocal recovery by *each carrier* of costs associated with the transport and termination *on each carrier's network facilities . . .*" (emphasis added). It is true that the term "costs" as used in section 252(d)(2) does not necessarily mean "actual costs" determined through "complex cost studies," but rather a "reasonable approximation of the additional costs of terminating" calls originating on another carrier's network. *SBC Inc. v. FCC*, 414 F.3d 486, 506-07 (3rd Cir. 2005). Current rules implementing this section clearly contemplate rates for reciprocal compensation will be set by reference to the individual carriers' costs of providing service. *See, e.g.*, 47 C.F.R. § 51.711(a); *see also Cost-Based Terminating Compensation for CMRS Providers; Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers; Implementation of the Local Competition Provisions of the Telecommunications Act Of 1996;* and *Calling Party Pays Service Offering in the Commercial Mobile Radio Services*, Order, 18 FCC Rcd 18441 (2003), at ¶2.

[16] Possibly, Verizon seeks to have the Commission impose a nationwide default rate of $0.0007 on all carriers as a way of responding to the court's mandamus order on ISP traffic. But as Verizon itself has exhaustively explained, the Commission has ample ability to respond to the D.C. Circuit's request for a better explanation of the legal rationale for imposing a $0.0007 rate cap on ISP-bound traffic without necessarily applying a uniform rate to other types of traffic. *See* Supplemental Comments of Verizon and Verizon Wireless on Intercarrier Payments for ISP-Bound Traffic and the Worldcom Remand, CC Docket Nos. 01-92, 96-98, and 99-68 (Oct. 2, 2008). *See also* Letter from Andrew D. Crain, Qwest, to Marlene H. Dortch, FCC, CC Docket Nos. 96-98, 99-68 and 01-92 (Sept. 24, 2008); Letter from Christopher J. Wright and John Nakahata, Harris, Whilshire and Grannis (Counsel to Level 3), to Marlene H. Dortch, FCC, CC Docket Nos. 99-68 and 01-92, (May 7, 2008); Letter from Robert W. Quinn, AT&T, to Chairman Martin, FCC, CC Docket No. 01-92 (July 17, 2008).

[17] Basic economics texts make clear that government-imposed, below-market prices hurt consumers by creating artificial shortages. The classic example is rent control in New York City, where housing shortages and abandoned buildings can be directly traced to government mandated rent controls. *See, e.g.*, Frank and Bernanke, Principles of Macroeconomics 2nd edition, McGraw-Hill 2004, pp. 58, 67-68. Imposing artificially low switched access rates would lead to an analogous situation in the telecommunications industry, causing inefficient routing of traffic and congestion. Interconnecting carriers would find it cheaper to abandon efficient dedicated transport arrangements in favor of common transport, which in turn would impose unnecessary costs on rural ILECs who must add transport capacity to trunk groups to meet government-imposed quality standards, diverting investment funds better spent on deploying broadband services.

[18] For example, rules establishing a default rate of $0.0007 would undoubtedly prompt large end users to seek "carrier" status to take advantage of below-cost interconnection pricing. Revised rates may also impose significant network rearrangement costs as carriers discontinue dedicated transport services in favor of below-cost switched transport services.

[19] *See Rural Alliance*, presentation at 5.

[20] *Id. See also* Letter from Tony Clark, Commissioner and Chair, NARUC Committee on Telecommunications, Ray Baum, Commissioner and Chair, NARUC Task Force, and Larry Landis, Commissioner and Vice-Chair, NARUC Task Force, to Kevin Martin, FCC, CC Docket No. 01-92 (July 24, 2006) (attaching the Missoula Plan). Other parties have likewise

NECA agrees with the Rural Alliance[21] that the Commission can best accomplish these objectives by permitting rate-of-return carriers to charge tariffed originating and terminating access rates unified at the interstate level.[22] To the extent reform brings about reductions in intercarrier compensation levels that cannot reasonably be recovered from end users, a sustainable, long-term alternative recovery mechanism must be put in place to assure rural rate-of-return carriers can continue to provide state-of-the-art services to rural consumers without disruptions or reductions in service quality.[23]

Finally, while Verizon and other interested parties have offered various proposals and legal theories supporting their preferred approaches to intercarrier compensation reform, it bears noting the Commission has not *itself* explained what options it is seriously considering or what specific actions and rules it plans to adopt.[24] This makes it difficult to analyze implementation details of potential Commission reform decisions. As the Commission determines what specific actions it plans to take, NECA stands ready to assist it in developing specific methods to assure a smooth transition for rural rate-of-return carriers to a revised intercarrier compensation regime.

Respectfully submitted,

Richard A. Askoff

Cc: Matthew Berry
Ajit Pai
Christopher Killion
Paula Silberthau
Don Stockdale
Randy Clarke
Marcus Maher
Jeremy Marcus
Al Lewis

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suggested using tier-based rate structures based on cost and operational differences among groups of carriers. *See, e.g.*, Letter from Curt Stamp, ITTA to Marlene H. Dortch, FCC, CC Docket No. 01-92 (Sept. 19, 2008) (attaching ITTA proposal).

[21] *Rural Alliance*, presentation at 5.

[22] Contrary to claims by Verizon and other large carriers, small rural rate of return ILECs do not have the resources or negotiating power to base access rates on "commercial negotiations." *See id.* at 4.

[23] *Id.* at 7-8.

[24] The Commission issued a notice of proposed rulemaking in 2001 discussing the possibility of replacing today's "calling party network pays" structure with a "bill and keep" system. *Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Notice of Proposed Rulemaking, 16 FCC Rcd 9610 (2001), at ¶ 19. A second NPRM, issued in 2005, described several alternative ICC reform concepts and plans advanced by various industry groups. *see* Further Notice of Proposed Rulemaking, 20 FCC Rcd 4685 (2005), at ¶¶ 37-62, but pointedly did *not* invite comment on a staff proposal for bill and keep. *Id.* at n. 106. The Commission has also received comment on the Missoula Plan, and its subsequent invitation to "refresh the record" in these dockets has produced a bewildering variety of reform proposals. The Commission's views, however, remain unknown.

TAB G

NTCA

The Voice of Rural Telecommunications
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October 6, 2008

Ms. Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, SW, TW-A325
Washington, D.C. 20554

***Ex Parte* Notice: *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92; and *IP-Enabled Services*, WC Docket 04-36.**

Dear Ms. Dortch:

On Thursday, October 2, 2008, Daniel Mitchell with the National Telecommunications Cooperative Association (NTCA) along with Charlie Cooper with Consortia Consulting and Jeff Reynolds with Reynolds Schultheis Consulting, Inc., met with Matthew Berry, Ajit Pai, Christopher Killion and Lisa Gelb with the FCC's Office of General Counsel to discuss issues raised in the above referenced dockets. Specifically, NTCA refuted the Verizon September 19, 2008, ex parte filing which erroneously claims the Commission has legal authority to adopt a $0.0007 terminating access rate for all traffic on the public switched communications network (PSTN), for all carriers, and in all jurisdictions. NTCA will discuss briefly in this filing the substance of the meeting and several reasons why the Commission should reject the $0.0007 proposal and Verizon's legal arguments. NTCA will file a more comprehensive legal brief in direct response to Verizon's September 19, 2008, filing in the next few days. In addition, enclosed please find a document which addresses several of Verizon's factual misrepresentations in its September 19, 2008 filing and NTCA's corrections to these misrepresentations. Also, enclosed please find NTCA's presentation concerning a numbers-based universal service contribution methodology also discussed in the meeting.

In the midst of the worst financial crisis since the Great Depression, Verizon, AT&T and others are desperately attempting to pull the wool over the eyes of the Federal Communications Commission (Commission or FCC), Congress, and the American Public in order to gain an unlawful multi-billion dollar annual windfall at the expense of consumers and small rural independent communications carriers.[1] Under the guise of solving regulatory arbitrage and fraud issues, Verizon erroneously asserts that the Commission has legal authority to preempt State Commission jurisdiction and to set a one-size fits all unified $0.0007 per minute terminating access rate for all voice traffic that is transported and terminated on the PSTN, by all carriers, and in all jurisdictions (Federal, State, and Local).[2] The unraveling of Verizon's contorted legal arguments reveals that Congress granted State Commissions, not the FCC, the exclusive legal authority to regulate and set intrastate toll access rates and local reciprocal compensation rates. The Verizon/AT&T $0.0007 proposal and its resulting multi-billion dollar annual windfall must be denied. Consumers must be spared the additional financial burden of paying for Verizon's and AT&T's unjust enrichment scheme while

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[1] See the AT&T, Verzion, et al Ex Parte filed on August 6, 2008, *In the Matter of a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92: *IP-Enabled Services*, WC Docket No. 04-36: *Universal Service Contribution Methodology*, WC Docket No. 06-122.

[2] See Verizon's Written Ex Parte Filed on September 19, 2008, *In the Matter of a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92: *IP-Enabled Services*, WC Docket No. 04-36: *Universal Service Contribution Methodology*, WC Docket No. 06-122. (Verizon Ex Parte, September 19, 2008).

at the same time having to pay for the Wall Street disaster under the Government's pending taxpayer bailout plan.

STATE COMMISSIONS HAVE EXCLUSIVE JURISDICTION TO SET AND REGULATE INTRASTATE ACCESS RATES AND RECIPROCAL COMPENSATION RATES

Section 152(b) of the Act provides the State Commissions with exclusive jurisdiction over intrastate rates and services. In *Louisiana Public Service Commission v. FCC* the Supreme Court specifically found that Section 152(b) "denies the FCC the power to preempt state regulation of depreciation for intrastate ratemaking purposes."[3] Indeed, the Supreme Court held:

> [Section 152(b)] asserts that "nothing in this chapter shall be construed to apply or give the Commission jurisdiction with respect to (1) charges, classifications, practices, facilities, or regulations for or in connection with intrastate communications service...." **By its terms this section fences off from the FCC reach or regulation intrastate matters-indeed, including matters "in connection with" intrastate service.** Moreover, the language with which it does so is certainly as sweeping as the wording of the provision declaring the purpose of the Act and the role of the FCC.[4] [Emphasis Added]

In 1999, the Supreme Court in *AT&T Corp. v. Iowa Utilities Board* affirmed this finding and stated that need for both limitations [federal and state] is exemplified by *Louisiana Public Service. Commission v. FCC*, where the FCC claimed authority to issue rules governing depreciation methods applied by local telephone companies.[5]

In *AT&T Corp. v. Iowa Utilities Board*, the Commission supported its claim of preemption of depreciation methods with two arguments. First, that it could regulate intrastate because Congress had intended the depreciation provisions of the Communications Act to bind state commissions--*i.e.*, that the depreciation provisions "applied" to intrastate ratemaking.[6] The Supreme Court observed that "[w]hile it is, no doubt, possible to find some support in the broad language of the section for respondents' position, we do not find the meaning of the section so unambiguous or straightforward as to override the command of § 152(b) ...."[7] The Commission also argued that, even if the statute's depreciation provisions did not apply intrastate, regulation of state depreciation methods would enable it to effectuate the federal policy of encouraging competition in interstate telecommunications.[8] The Supreme Court also rejected that argument because, even though the FCC's broad regulatory authority normally would have been enough to justify its regulation

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[3] *Louisiana Public Service Commission v. FCC*, 106 S.Ct. 1890, 476 U.S. 355, 90 L.Ed.2d 369, 54 USWL 4505, p. 12, (May 27, 1986).

[4] Id., at 54 USWL 4505, p. 11.

[5] *AT&T Corp. v. Iowa Utilities Board*, 525 U.S. 366, 119 S.Ct. 721 (Jan 25, 1999), see, http://www.fcc.gov/ogc/documents/opinions/1999/iowa.html, p.7 of 36.

[6] See, http://www.fcc.gov/ogc/documents/opinions/1999/iowa.html, p.7 of 36.

[7] Id.

[8] Id.

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of intrastate depreciation methods that affected interstate commerce,[9] Section 152(b) prevented the Commission from taking intrastate action solely because it furthered an interstate goal.[10]

Although the precise issue of whether the Commission has authority to establish a single $0.0007 per minute terminating access default rate for all traffic, for all carriers, in all jurisdictions was not raised in *AT&T Corp. v. Iowa Utilities Board,* the Supreme Court stated the following:

> The FCC's prescription, through rulemaking, of a requisite pricing methodology no more prevents the States from establishing rates than do the statutory 'Pricing Standards' set forth in Section 252(d). ***It is the States that will apply those standards and implement that methodology, determining the concrete result in particular circumstances. That is enough to constitute the establishment of rates.***[11] [Emphasis added]

Appropriately, the Supreme Court determined the FCC has the authority to establish the pricing methodology and the State Commissions have the explicit authority pursuant to Section 251 and 252 to actually determine the reciprocal compensation rates for each particular carrier based on their own unique costs and circumstances. Thus, the FCC cannot use its pricing methodology authority to establish a one-size fits all default $0.0007 terminating access rate that will apply to all traffic, to all carriers, in all jurisdictions. This would be a direct violation of Sections 152(b), 251(b)(5), 251(d)(3), and 252(d). The FCC's establishment of the all-encompassing $0.0007 rate would divest the State commissions of their authority to set rates and to determine "concrete result[s] in particular circumstances." Accordingly, the mandatory $0.0007 proposal must be dismissed.

PREEMPTION

Verizon ignores *Louisiana Public Service Commission v. FCC*, and fails to address the critical finding in *AT&T Corp. v. Iowa Utilities Board* that prohibits the FCC from setting a one-size fits all default terminating access rate. Instead, Verizon asserts that the Supremacy Clause of Article VI of the United States Constitution provides the FCC with the power to preempt state commission jurisdiction and ratemaking authority under Sections 152(b), 251(b)(5), 252(d)(2)(A)(ii), and 252(d)(2)(B)(ii) of the Act. Verizon is wrong and is attempting to mislead the Commission.

Congress, in enacting the Communications Act of 1934, as amended, did not "express a clear attempt to preempt state law."[12] To contrary, Congress expressly preserved State Commission jurisdiction over charges, classifications, practices, facilities, or regulations for or in connection with intrastate communications services pursuant to Section 152(b). Indeed, Congress enhanced State Commission jurisdiction in 1996, when it amended the Communications Act of 1934 with Section 251(d)(3) entitled in capital letters by Congress the "PRESERVATION OF STATE ACCESS REGULATIONS." Section

[9] See *Louisiana Public Service Commission v. FCC*, 476 U.S. at 377, 106 S.Ct. 1890; cf. *Houston & Shreveport R. Co. v. United States*, 234 U.S. 342, 358, 34 S.Ct. 833, 58 L.Ed. 1341 (1914).
[10] *Louisiana Public Service Commission v. FCC*, 476 U.S. at 377, 106 S.Ct. 1890.
[11] See, http://www.fcc.gov/ogc/documents/opinions/1999/iowa.html, p.8 of 36.
[12] *Jones v. Rath Packing Co.*, 430 U.S. 519, 97 S.Ct. 1305, 51 L.Ed. 604 (1977).

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251(d)(3) states that in "prescribing and enforcing regulations to implement the requirements of this section, the Commission shall not preclude the enforcement of any regulation, order, or policy of a State Commission that -

(A) Establishes access and interconnection obligations of local exchange carriers;
(B) Is consistent with the requirements of this section; and
(C) Does not substantially prevent the implementation of the requirements of this section and the purposes of this part."

Furthermore, Section 251(b)(5) explicitly provides the State Commissions with the legal "duty to establish reciprocal compensation arrangements for the transport and termination of Telecommunications" for voice calls that originate and terminate in a local calling area shared by two competing carriers.[13] Thus, Congress has expressly directed that the State Commissions, and not the FCC, shall exercise jurisdiction over charges, classifications, practices, facilities, or regulations for or in connection with intrastate communications services, including local reciprocal compensation.[14]

In addition, there is no outright or actual conflict between federal and state law.[15] Congress has clearly established that the FCC has jurisdiction over interstate (Federal) communications pursuant to Section 151, and State Commissions have jurisdiction over intrastate (State) and reciprocal compensation (local) communications pursuant to Sections 152, 251, and 252 of the Act. These jurisdictional and authoritative boundaries have worked together since 1934 and have flourished throughout the 1990s and 2000s in establishing vibrant competitive communications markets that have lead to new and innovative services, new jobs, and opportunities for new entrants and consumers. Indeed, compliance with both federal and state intercarrier compensation laws and regulations has never been nor is it now physically impossible to implement and enforce.[16]

Moreover, there is nothing in Federal law, implicit or explicit, which provides a barrier to State Commissions to set intrastate (state) toll access rates or reciprocal compensation (local) access rates[17] nor has Congress legislated comprehensively, thus occupying an entire field of regulation and leaving no room for the States to supplement federal law.[18] Indeed, as demonstrated above and below the Act itself pursuant to sections 152(b), 251(b)(5), 251(d)(3), 252(d)(2)(A)(ii), and 252(d)(2)(B)(ii)

[13] Section 252(d)(2)(B) states that this paragraph shall not be construed - to precluded under Section 252(d)(2)(B)(i) arrangements that afford the mutual recovery of costs through the offsetting of reciprocal obligations, including arrangements that waive mutual recovery (such as bill-and-keep arrangements); or to authorize under 252(d)(2)(B)(ii) the Commission or any State commission to engage in any rate regulation proceeding to establish with particularity the additional costs of transporting or terminating calls, or to require carriers to maintain records with respect to additional costs of such calls.
[14] Section 252(b)(2)(A) states for the purpose of compliance by an incumbent local exchange carrier with section 251(b)(5), a State commission shall not consider the terms and conditions for reciprocal compensation to be just and reasonable – (i) such terms and conditions provide for the mutual and reciprocal recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of another carrier; and (ii) such terms and conditions determine such costs on the basis of a reasonable approximation of the traditional costs of terminating such calls.
[15] *Free v. Bland*, 369 U.S. 663, 82 S.Ct. 1089, 8 L.Ed. 180 (1962).
[16] *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 312, 83 S.Ct. 1210, 10 L.Ed. 284 (1963).
[17] *Shaw v. Delta Airlines, Inc.*, 463 U.S. 85, 103 S.Ct. 2890, 77 L.Ed. 4909 (1983)
[18] *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 67 S.Ct. 1146, 91 L.Ed. 1447 (1947).

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explicitly provides multiple barriers which prevent the FCC, not State Commissions, from setting intrastate (state) toll access rates and reciprocal compensation (local) access rates.

Verizon further argues that sections 152(b), 251(b)(5), 251(d)(3), 252(d)(2)(A)(ii), and 252(d)(2)(B)(ii) stand as an obstacle to the accomplishment and execution of the full objectives of Congress, and thus the FCC should preempt State Commission jurisdiction to set and regulate intrastate access charges and reciprocal compensation rates.[19] As shown below Verizon's arguments are self-serving, misleading and without merit.[20]

Verizon asserts that prevention of arbitrage and fraud provides the basis for the FCC to assert preemption and the need for a uniform rate of $0.0007 per minute.[21] Verizon claims that different rates are an obstacle to competition, investment, and deployment of new services.[22] These arguments are wrong. Competition particularly from wireless has flourished under the current regulatory regime. New services and investment have blossomed under this regulatory regime. The record does not contain evidence, much less substantial evidence that going to a uniform rate wound increase competition, investment, or new services in the communications industry.

Indeed, the Commission's most recent report on the state of competition in the wireless industry using a new data source that allows for a significantly more granular and accurate analysis of mobile telephone service deployment and competition found that:

- Approximately 280 million people, or 99.8 percent of the U.S. population, have one or more different operators offering mobile telephone service in the census blocks in which they live.
- More than 95 percent of the U.S. population lives in areas with at least three mobile telephone operators competing to offer service.
- More than half of the U.S. population lives in areas with at least five competing mobile telephone operators.
- Approximately 99.3 percent of the U.S. population living in rural counties, or 60.6 million people, have one or more different operators offering mobile telephone service in the census blocks within the rural counties in which they live.

[19] Verizon Ex Parte, September 19, 2008, pp. 19-26, 29-35.
[20] *Hines v. Davidowitz*, 312 U.S. 52, 61 S.Ct. 399, 85 L.Ed. 581 (1941). Preemption may result not only from action taken by Congress itself; a federal agency acting within the scope of its congressionally delegated authority may preempt state regulation. *Fidelity Savings & Loan Assn. v. De la Cuesta*, 485 U.S. 141, 102 S.Ct. 3014, 73 L.Ed. 664 (1982); *Capital Cities Inc.*, 467 U.S. 691, 104 S.Ct. 2964, 81 L.Ed. 580 (1984).
[21] Verizon Ex Parte, September 19, 2008, p. 28.
[22] Id., pp. 26-28.

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- Approximately 82 percent of the U.S. population lives in census blocks with at least one mobile broadband provider offering service.[23]

In addition, during 2006, the number of mobile telephone subscribers in the United States rose from 213 million to 241.8 million, increasing the nationwide penetration rate to approximately 80 percent. The average amount of minutes that subscribers spend using their mobile devices increased from 708 minutes per month during the second half of 2005 to 714 minutes per month during the second half of 2006. In addition, the volume of text messaging traffic rose from 9.8 billion messages sent during December 2005 to 18.7 billon messages sent during December 2006. Revenue per minute, which can be used to measure the per-minute price of mobile telephone service, remained unchanged during 2006 at $0.07.[24] As the foregoing data illustrates, new services and investment are flourishing under today's federal/state access charge regime.

Verizon claims further that the FCC should preempt state jurisdiction over state and local access charges because carriers cannot or will not be able to determine the federal/state/local jurisdiction of the majority voice traffic in the future.[25] In other words, landline, wireless and Internet voice traffic today and in the future will be "inseverable."[26] This is also untrue. Today, the overwhelming majority of voice traffic is separated, categorized and jurisdictionalized. In 2007, there were 15 billion identified and jurisdictionalized interstate (federal) access minutes according to the National Exchange Carrier Association (NECA) Access Service Tariff F.C.C. No. 5. Transmittal No. 1214, Volume 3, page 4, submitted to the Commission on June 16, 2008. Billing between carriers for originating and terminating voice calls in all jurisdictions – federal, state, and local - is estimated at approximately $8 billion dollars per year. If these voice calls were inseverable, unbillable, and unrecoverable as alleged by Verizon, the industry would have come to a screeching halt a long- time ago.

Instead the opposite is happening in the communications market under the existing federal/state access charge regime. Markets for access today are extremely competitive and opportunities to raise federal and state access rates are prohibited and constrained by competition. The correct conclusion, as the then BellSouth, now AT&T, noted with respect to special access, is for the federal government not to regulate and certainly not for the federal government to insist on uniform rates.[27] In 2005, competition for special access flourished driving rates down. The same arguments apply with respect to the switched access market today. Wireless and VoIP traffic have flourish under the current federal/state regulatory regime. Current federal/state regulation is not an impediment to competition, to new investment, or to new broadband services. There is no need for the government to change the regulatory structure to achieve the FCC's and

[23] FCC Release Annual Report on State of Competition in the Wireless Industry (FCC 08-28), New Release, February 4, 2008. http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-279986A1.doc.
[24] Id.
[25] Verizon Ex Parte, September 19, 2008, pp. 3-4.
[26] Id.
[27] Comments of BellSouth, *In the Matter of Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25. *AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM 10593, pp. 13-19, filed on June 13, 2005. See. http://fjallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6517632863.

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Congress' stated policy goals. Those goals are being achieved under the current federal/state access structure.[28]

Verizon also claims that IP-based service offerings "up-end traditional conceptions of location-based and device-based phone numbers" and "eliminate the historical understanding that a 'call' has only two end points."[29] Verizon states that wireless services break the "historical connection between telephone numbers and geographic location."[30] Verizon further states that a telephone number is no longer a reliable indicator of the geographic location of a user of IP-based or wireless services *implies that* such services are "location-independent."[31] All of these assertions are false.

The Internet protocol is, above all else, an *end-to-end* addressing scheme designed expressly for the purpose of exchanging data between two parties,[32] where each party's customer premise equipment CPE knows the IP address of the other, and where ***both addresses are present in every data packet sent*** between them. Public Internet addresses are well-defined within the address space specified by the Internet Corporation for Assigned Names and Numbers (ICANN), a non-profit organization, under the terms of its contract with the U.S. Department of Commerce. Every assigned IP address – whether public or private – is unambiguously associated with a single, specific electronic device, which necessarily resides in a particular geographical location. Further, the facts that (a) every IP data packet contains both a source address and a destination address and (b) the primary task of an IP network is to deliver these packets from their source CPE to their destination CPE together refute the assertion that IP-based communications do not have two end points.

The only ambiguities in associating an IP address with the exact physical location of a device occur either when the device is using wireless Internet access or the device utilizes Dynamic Host Configuration Protocol ("DHCP") to obtain an Internet address from a pool of addresses kept by a DHCP server. Yet even in those cases, the uncertainty in a device's exact location might only very rarely rise to a level that would preclude the association of an Internet address with the State in which the equipment is located.

The assertion that IP-based services or wireless services somehow operate independently of the physical transmission of information-bearing signals between electronic devices – including end users' devices, which obviously exist in real, physical space and are located at some real, geographical location – is simply false.

Verizon also argues that subjecting VoIP and other IP-based services to state regulations designed for different services in a different era would thus conflict with Congress's and the Commission's policies to encourage the development and deployment of broadband services, as set forth in Section 706 of the 1996

[28] See, *Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable And Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996,* GN Docket No. 07-45, Report (rel. June 12, 2008) (Fifth 706 Report); Also see, *12th Annual CMRS Competition Report, Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993: Annual Report and Analysis of Competitive Market Conditions with Respect to Commercial Mobile Services,* Report FCC 08-28, (Released February 4, 2008).
[29] Verizon Ex Parte, September 19, 2008, p. 5.
[30] Verizon Ex Parte, September 19, 2008, p. 6.
[31] Verizon Ex Parte, September 19, 2008, p. 9-10.
[32] *See* Robert Cannon, "Will the Real Internet Please Stand Up: An Attorney's Quest to Define the Internet" (March 2004) at pages 8-9. Telecommunications Policy Research Conference 2002. Html version available at http://intel.si.umich.edu/tprc/papers/2002/165/RealInternet.htm.

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Act.[33] Verizon is wrong once again. In FCC's August 5, 2008 amicus brief in *Vonage v. Nebraska Public Service Commission,* the FCC recognized that a portion of VoIP service revenue is properly classified as intrastate in nature and thus can be separated and assessed for state universal service funding (USF) purposes.[34] If interconnected VoIP traffic can be separated and accessed for USF purposes, it can properly be separated, jurisdictionalized and billed for access charges in the federal and state jurisdictions.

Verizon further claims that under today's federal/state access rate regime stands as an obstacle to the FCC's policies to encourage the deployment of broadband as set forth in Section 706 of Act.[35] This claim is false. In June 2008, the Commission submitted its Fifth Section 706 Report to Congress on the status of broadband deployment throughout the United States. In this Report, the FCC concluded that advanced telecommunications capability is being deployed to all Americans in a reasonable and timely fashion and therefore the FCC is not required to take "immediate action" to rectify any failure.[36] Verizon's argument that the current federal/state access regime stands as an obstacle to the accomplishment and execution of the objectives of Congress in Section 706 of the Act, falls on its face in light of the FCC's most recent Section 706 findings and Report to Congress.

FORBEARANCE:

Verizon argues that if the Commission is prohibited from establishing a single $0.0007 per minute terminating access rates for all traffic, for all carriers, and in all jurisdictions, then in the alternative the FCC should "forbear from Section 251(b)(5) traffic (local reciprocal compensation traffic) and regulate such traffic directly" because it is inseverable, and then set the rate for this traffic at $0.0007 per minute.[37] Verizon's alternative legal argument is flawed in many respects, the most glaring is the fact the Commission can not forbear from enforcing a section of the Act for which the FCC does not possess Congressionally-delegated jurisdiction or enforcement authority.

As demonstrated above, the FCC does not have legal authority to set rates under Section 251(b)(5). Section 251(b)(5), when read in conjunction with Section 252, explicitly provides the State Commissions with the legal "duty to establish reciprocal compensation arrangements for the transport and termination of telecommunications" for voice calls that originate and terminate in a local calling area shared by two competing carriers. Congress has expressly delegated to the State Commissions, to the exclusion of the FCC (unless the State Commission fails to act, in which case, *and only in which case*, Congress authorized action by the FCC pursuant to Section 252(e)(5)) jurisdiction over charges, classifications, practices, facilities, or regulations for or in connection with intrastate communications services, including reciprocal compensation.

---

[33] Verizon Ex Parte, September 19, 2008, p. 14.
[34] *Brief of Amicus Curiae United States and Federal Communications Commission Supporting Appellant's request for Reversal, In the United States Court of Appeals For the Eight Circuit, No. 08-1764, Vonage Holdings Corp. and Vonage Network Inc., v. Nebraska Public Service Commission et al.* on Appeal form the United States District Court for the District of Nebraska, filed on August 5, 2008 at pp. 16-17.
[35] Verizon Ex Parte, September 19, 2008, pp. 26-28.
[36] *See Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable And Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996,* GN Docket No. 07-45, Report (rel. June 12, 2008) (Fifth 706 Report).
[37] Verizon Ex Parte, September 19, 2008, pp. 26-29.

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Thus, the FCC cannot forbear from enforcing a section of the Act for which the FCC does not possess Congressionally-delegated jurisdiction or enforcement authority.

Further, Section 251(b)(5) only applies to traffic for calls that originate and terminate in a local calling area shared by two competing carriers. For a wireline to wireline carrier call this is a local area within a State's borders. For an intrastate toll call – a call that originates in the local calling of one carrier and terminates in a different local calling area of another carrier, but both local calling areas located within the same State's borders – the FCC has no jurisdiction to set the rates for such intrastate toll calls. Section 152(b) provides the State Commissions with exclusive jurisdiction over these calls as demonstrated above and confirmed by the Supreme Court.[38] Again, the FCC cannot forbear from enforcing a section of the Act which it does not have jurisdiction and authority to enforce.

Moreover, under the Act's forbearance provision, 47 U.S.C. Section 160(a), the FCC may forbear from applying a regulation or provision of the Act, if the Commission determines that the enforcement of such regulation is: (a) "not necessary to ensure that the charges, practices, classifications, or regulations . . . are just and reasonable and not unjustly or unreasonably discriminatory", (b) "enforcement of such regulation or provision is not necessary for the protection of consumers", and (c) "forbearance from applying such provision or regulation is consistent with the public interest" Notwithstanding the fact that FCC cannot set local reciprocal compensation rates under Section 251(b)(5) or set intrastate toll rates under section 152(b), if State Commissions were prohibited from setting and enforcing access rates established under Sections 251(b)(5) and 152(b), consumers living rural areas of the United States served by rate-of-return (RoR) carriers would see their voice and broadband rates increase to unjust and unreasonable levels, their financial ability to purchase broadband become limited or prohibited, and the Congress's goals of competition, investment, and broadband deployment would grind to halt in rural America.

Today, for billions of landline, wireless, and VoIP minutes, the end points are determinative and can be accurately billed. Verizon obfuscates the true question of severability; that is "can the end points of a call be determined and on that basis does traffic have a jurisdictional nature" and the clear answer is yes; traffic is severable. Verizon clearly admits that the true location of the end points of a transmission can be determined with the proper equipment and real time systems.[39] The Commission itself supported this position concerning interconnected VoIP in its amicus brief filed in support of the *Nebraska Public Service Commission in Vonage v. NPSC*, No. 08-1764 (8th Cir.), pages 16-17, August 5, 2008. Verizon's premise that the FCC can forbear from regulation of an area for which it does not possess congressionally delegated regulatory authority is flawed. In addition, Verizon's inseverability argument is contrary to the FCC's recognition that intrastate and interstate elements of interconnected VoIP service can be severed for purposes of universal service contributions as indicated in the FCC's amicus brief and in the Commission's interconnected VoIP universal service contribution order.[40]

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[38] *Louisiana Public Service Commission v. FCC*, 106 S.Ct. 1890, 476 U.S. 355, 90 L.Ed.2d 369, 54 USWL 4505, p. 12, (May 27, 1986).
[39] Verizon Ex Parte, September 19, 2008, p. 17.
[40] Universal Service Fund Contribution Methodology, 21 FCC Rcd 7518 (2006)., *aff'd in part and rev'd in part, Vonage Holdings Corp v. FCC*, 489 F.3rd 1232 (D.C. Cir. 2007).

In summary, the Commission does not have the statutory authority to set intrastate rates, reciprocal compensation rates, or preempt State Commission jurisdiction to regulate these rates. As state above, NTCA will file a more comprehensive legal brief in response to Verizon's September 19, 2008 filing, in the next few days. Pursuant to Section 1.1206 of the Commission's rules, a copy of this letter is and the document which addresses several of Verizon's factual misrepresentations in its September 19, 2008 filing and NTCA's corrections to these misrepresentations is being filed via ECFS with your office. If you have any questions. please do not hesitate to contact me at (703) 351-2016.

Sincerely,

/s/ Daniel Mitchell
Daniel Mitchell
Vice President
Legal and Industry

DM:rhb
Enclosure

cc:
Matthew Berry
Ajit Pai
Paula Silberthau
Christopher Killion
Lisa Gelb
Albert Lewis
Rebekah Goodheart

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Ex Parte Handout

VERIZON'S FACTUAL MISREPRESENTATIONS
In Its September 19, 2008, Ex Parte Filing
CC Docket No. 01-92
WC Docket No. 04-36
WC Docket No. 06-122

Inseverability

Verizon

- For CMRS and VoIP based services there is no practical means to identify the "end points" of a call. (Verizon Ex parte Filing (VZ) p. 5-6)
- With "find-me" and "follow-me" services, telephone numbers are an increasingly poor proxy for location (VZ p. 9)
- Intermodal porting of a telephone number breaks the association between numbers and location (VZ p. 10)
- Carriers can't distinguish between technologies relative to intermodal traffic terminating on the PSTN (VZ p. 11)
- There is no service market driven reason to develop capabilities to identify the end points of traffic (VZ p. 12)
- Arbitrage is the outcome associated with disparate rates for all carriers (VZ p. 13)

The Reality

- Today, for hundreds of billions of minutes, the end points are determinative and can be accurately billed.
- Verizon obfuscates the true question of severability; that is "can the end points of a call be determined and on that basis does traffic have a jurisdictional nature" and the clear answer is yes; traffic is severable.
    - Verizon clearly admits that the true location of the end points of a transmission can be determined with the proper equipment and real time systems (VZ p. 17)
    - The FCC itself supported this position in its amicus brief filed in support of the Nebraska Public Service Commission in Vonage v. NPSC, No. 08-1764 (8th Cir.).
- It is unnecessary to discriminate between technologies to determine the end points of a call.
- End point identification is critical to the operation of public safety services (E-911) and law enforcement activities (CALEA)

Decline in Traditional Long Distance Services

Verizon

- Substitution on a massive scale is occurring for traditional wireline subscriptions and traditional long distance service (VZ p. 6-7)
    - Analysts report that VoIP providers have reached 31% of households
    - Government Health agency reports that 15.8% of households have fully cut cord
    - Traditional wireline access minutes have dropped from 792 billion minutes in 2000 to 544 billion in 2006 because of wireless and VoIP substitution
- Substitution trends will continue at an ever increasing rate (VZ p. 8)

The Reality

- The fact that there are fully 84.2% of households and 544 billion access minutes still associated with wireline service is reason enough for the Commission to not prematurely make draconian changes to the intercarrier compensation regime.
- In rural areas, the percentage of customers that have retained their wireline phone is higher than in urban areas because rural customers often do not have wireless service at their homes or even uninterrupted service along highways.
- Enterprise customers will always require services that meet carrier grade requirements including high levels of transmission quality and availability and will continue to be connected to the transport network via wireline QoS managed networks.
- Nearly all transport networks are landline.
- Most wireless carriers use the wireline network to transport their traffic, especially in rural areas.

Negotiated/Arbitrated Rates in Reciprocal Compensation Agreements

Verizon

- The $0.0007 per minute is the same rate currently applicable to a portion of § 251(b)(5) traffic as a result of the Commission's mirroring rule. (VZ p. 29)
- The $0.0007 per minute is consistent with Verizon's more recent experience in negotiating agreements with CLECs; Verizon has entered into negotiated and publicly filed interconnection agreements with a number of carriers, including AT&T and Level 3 that set a rate at or below $0.0007 per minute for terminating local traffic and for ISP-bound traffic. These agreements provide substantial evidence that $.0007 rates are just and reasonable because carriers have agreed to **them** through voluntary, arms-length negotiations (VZ p. 31).

The Reality

- Virtually no rural ILECs have adopted the $0.0007 rate and the mirroring rule.
- Per minute rates that range between $0.02 and $0.025 are consistent with rural **carriers'** experience in Nebraska, Iowa, and South Dakota in negotiating agreements with CMRS carriers. These negotiated or arbitrated rates constitute evidence that these rates for rural ILECs are just and reasonable.
    - Iowa-Over 270 interconnection agreements on file between rural ILECs and various CMRS carriers at $0.02
    - South Dakota-50 interconnection agreements on file between rural ILECs and CMRS carriers at rates that range between $0.02 and $0.03
    - Nebraska-38 interconnection agreements on file between rural ILECs and CMRS carriers at rates that range between $0.02 and $0.024.
- What Verizon cites as its additional terminating cost does not represent the reality of rural LECs and cannot be considered a just and reasonable terminating rate for rural LECs

<u>Concerns from the Economic Perspective</u>

Verizon

- Market outcomes provide strong evidence that $0.0007 per minute is a just and reasonable rate (VZ p. 5)
- ....prevent market forces from distributing limited investment resources to their most efficient uses (VZ p. 21)

The Reality

- If market forces were left alone to distribute investment resources to their most efficient uses, rural areas in the United States today would not have access to telecommunication or advanced services, such as broadband
- Since rural customers are an integral part of the telecommunication market, the costs of providing service to this market segment are part of the total economic costs of having an efficient telecommunication system.
- According to economic theory, the costs of correcting for a market failure should be internalized in the total cost of providing a particular good or service, in this case, telephone service.
- Differentiated rates from carrier to carrier for intercarrier compensation are efficient because they allocate resources according to various costs associated with conducting business in different geographies.
- It would not be responsible for the FCC to adopt an intercarrier compensation reform plan without conducting a complete cost-benefit analysis of switching from the current practice to Verizon's proposed plan.

- There are <u>multiple</u> economic concerns with Verizon's proposed plan
  - Verizon does not quantify the supposed benefits of its plan.
    - Verizon refers to the benefits of its plan as being simpler and easier to administer. Only anecdotal evidence is provided for how the proposed rate of $0.0007 per minute was determined.
  - According to Verizon, the Commission should adopt $.0007 for all traffic because Verizon negotiated some interconnection agreements at this rate.
    - The laws of supply and demand for the entire market should be used to determine the equilibrium price of any service.
    - When determined by the rules of the market, the prices of many goods and services (for example, gas food, electricity, and many others) vary regionally to reflect variations in cost. The price of interconnection (access and reciprocal compensation) should not be any different.
  - The Verizon proposal does not provide any information on the economic costs of the proposed plan.

<u>Other False Jurisdictional Issues raised by Verizon</u>

Verizon

- IP-based service offerings "up-end traditional conceptions of location-based and device-based phone numbers" and "eliminate the historical understanding that a 'call' has only two end points." (VZ p. 5)

- Wireless services break the "historical connection between telephone numbers and geographic location." (VZ p. 6)

- The fact that a telephone number is no longer a reliable indicator of the geographic location of a user of IP-based or wireless services ***implies that*** such services are "location-independent." (VZ p. 9-10, ***emphasis added***)

The Reality

- The Internet protocol is, above all else, an *end-to-end* addressing scheme designed expressly for the purpose of exchanging data between two parties,[1] where each party's CPE knows the IP address of the other, and where ***both addresses are present in every data packet sent*** between them. Public Internet addresses are well-defined within the address space specified by the Internet Corporation for Assigned Names and Numbers (ICANN), a non-profit organization, under the terms of its contract with the U.S.

[1] *See* Robert Cannon, "Will the Real Internet Please Stand Up: An Attorney's Quest to Define the Internet" (March 2004) at pages 8-9. Telecommunications Policy Research Conference 2002. Html version available at http://intel.si.umich.edu/tprc/papers/2002/165/RealInternet.htm.

Department of Commerce. Every assigned IP address – whether public or private – is unambiguously associated with a single, specific electronic device, which necessarily resides in a particular geographical location. Further, the facts that (a) every IP data packet contains both a source address and a destination address and (b) the primary task of an IP network is to deliver these packets from their source CPE to their destination CPE together refute the assertion that IP-based communications do not have two end points.

- The only ambiguities in associating an IP address with the exact physical location of a device occur either when the device is using wireless Internet access or the device utilizes Dynamic Host Configuration Protocol ("DHCP") to obtain an Internet address from a pool of addresses kept by a DHCP server. Yet even in those cases, the uncertainty in a device's exact location only rarely rises to a level that would preclude the association of an Internet address with the state in which the equipment is located.

- The assertion that IP-based services or wireless services somehow operate independently of the physical transmission of information-bearing signals between electronic devices – including end users' devices, which obviously exist in real, physical space and are located at some real, geographical location – is simply false.

Verizon

Terminating LECs cannot reliably distinguish IP-based from circuit-switched incoming traffic, nor can they reliably identify the geographical location of the calling party by examining the Calling Number associated with an individual incoming call.

Reality

- While LECs cannot do such identification, this is *irrelevant* to the question of whether calls are originated from an identifiable geographic location and can therefore, in principle, be classed as interstate or intrastate calls.

Verizon

- The Commission found in the *Vonage Order* that all Voice over Internet Protocol ("VoIP") *traffic* is inseverable and, therefore, interstate for jurisdictional purposes. (VZ, p. 3; *emphasis added)*

Reality

- The Commission found no such thing. In the *Vonage Order*, the Commission found there was no possibility of separating Vonage's *service* – not its traffic – into interstate and intrastate components so as to allow the Minnesota PUC to exert control over only the intrastate service while leaving the interstate service under federal control. The Commission made no such determination with respect to VoIP *traffic*.

Verizon

- IP traffic provides a particularly clear example of traffic that is jurisdictionally mixed, but inseverable for jurisdictional purposes and for which the Commission must establish a uniform federal regime. (VZ p. 18)

Reality

- IP traffic is not jurisdictionally mixed. Just like circuit-switched voice traffic, some is interstate and some is intrastate. VoIP *services*, however, are jurisdictionally mixed, and the FCC preempted state commissions from exercising authority over such *services*.

- The FCC recently supported the Nebraska Public Service Commission's requirement that Vonage and other VoIP providers contribute to **Nebraska's** universal service fund on the basis of Vonage's intrastate revenues (See Vonage v. NPSC, No. 08-1764 (8th Cir.))

NTCA

NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION

The Voice of Rural Telecommunications

www.ntca.org

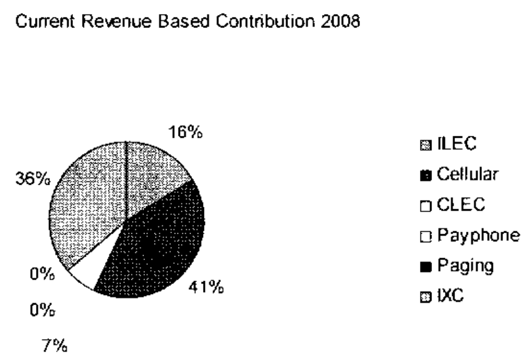
Universal Service Contribution Shifts

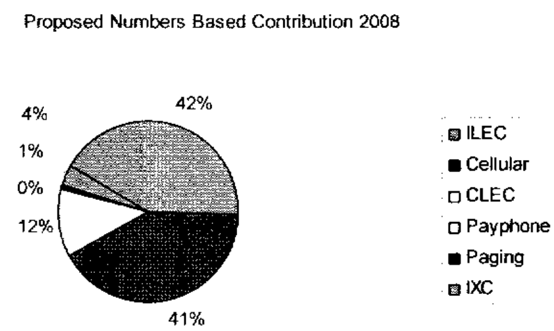
Impacts of moving from a revenue based to a numbers based universal service contribution plan

October 2, 2008

Comparison of Revenues and Numbers Based Contributions

Distribution Percentage

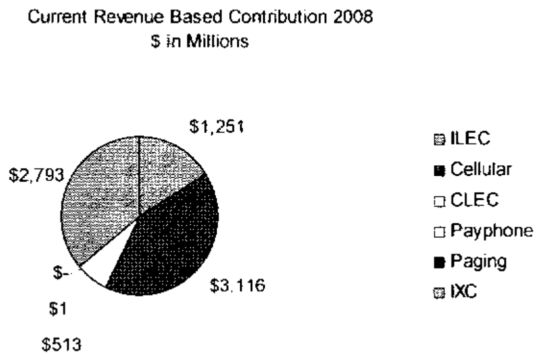


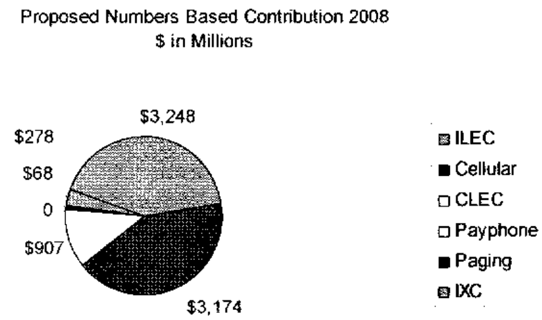


October 2, 2008

Comparison of Revenues and Numbers Based Contributions

Dollars





October 2, 2008

Increases & Decreases

Largest Decrease:

- IXCs:
  - $2.5B Decrease

Second Largest Decrease:*

- Cellulars:
  - $1.1B Decrease

Largest Increase:

- ILECs:
  - ALMOST $2B INCREASE

* If the FCC does not fully count each number, such as not counting each family plan number

October 2, 2008

Other Factors

- Companies w/ multiple lines of business (toll, wireless, wireline) are net winners
- The bigger the IXC portion, the bigger the savings i.e. IXC could become a “good” business (again)
- Number reporting is more “susceptible to manipulation” than revenues
  - Numbers “grooming” has not occurred

Additional Considerations

- Universal Service need could grow by $3B because of ICC changes and need for broadband deployment
- Numbers plan does not factor in the rapidly growing special access market

Conclusions

- Sustainability of rural wireline networks is at stake
- Triple “whammies” of reduced ICC, increased SLCs and increased USF contribution under a numbers scheme
- Large rate increases to wireline rural customers

CoBank
Rural America's Cooperative Bank

50 F Street, NW, Suite 900
Washington, District of Columbia 20001

September 30, 2008

Ms. Marlene H. Dortch, Secretary
Federal Communications Commission
Office of the Secretary
445 12th Street, SW
Washington, D.C. 20554

Ex Parte Notice

RE: Developing a Unified Intercarrier Compensation Regime
CC Docket No. 01-92

IP-Enables Services
WC Docket No. 04-36

Dear Ms. Dortch,

CoBank, ACB ("CoBank")[1] urges the Federal Communication Commission (the Commission) to proceed with the utmost care regarding the forthcoming ISP Remand Order. When addressing intercarrier compensation reform, it is critical to consider the rural consumers who rely on rural telecommunication carriers to receive their services. The Commission should ensure that all consumers have access to affordable telecommunications services and the latest technologies – no matter where they live. Technology is only useful when it is affordable to consumers.

CoBank is a cooperative bank with over $3.4 billion in loan commitments to over 200 rural communication companies nationwide. These commitments by sector are comprised of incumbent local exchange carrier (ILEC) (75%), wireless (11%), cable television (12%) and competitive local exchange carrier (2%). In addition, CoBank has syndicated $750 million of communication loans to other financial institutions in the Farm Credit System. The Farm Credit System is a unique cooperative network of customer-owned lending institutions that is exclusively dedicated to improving life in rural America.

[1] CoBank, a $62 billion Denver-based cooperative bank, provides financing to rural cooperatives and critical lifeline businesses – food, water, electricity and communications – across the United States. Part of the $208 billion United States Farm Credit System, the bank also finances agricultural exports. CoBank consistently demonstrates our focus on rural America. We consistently demonstrate our focus on rural America, repeatedly strive to be the trusted advisor for our customer-owners, provide a consistent return on their investment and ownership in CoBank.

In order to provide rural customers the communication services needed to compete in a global economy, rural ILECs rely upon high-cost universal support and intercarrier compensation for a substantial portion of their cost recovery. It is imperative that reform of the rules for these revenue streams take into account the unique characteristics of rural ILECs and their service areas.

CoBank is concerned that proposals like the AT&T and Verizon proposal on terminating access rate do not address the operating characteristics of rural ILECs. The AT&T and Verizon proposal on terminating access rate will make it difficult for rural ILECs to provide rural consumers with a full array of affordable basic and advanced communications services, comparable to price and quality to those offered in urban areas.

CoBank's rural communications customers are committed to providing innovative, high quality, vital infrastructure to meet the demands of its consumers. Our rural telecommunications customers need comprehensive reform of intercarrier compensation, not the adoption of piecemeal proposals.

Respectfully submitted,

CoBank, ACB

By: /s/ Robert S. West
Robert S. West
Senior Vice President and Manager, Communication Division

RTFC
RURAL TELEPHONE FINANCE COOPERATIVE
2201 Cooperative Way · Herndon, Virginia 20171-3025
703-709-6700

September 30, 2008

Chairman Kevin Martin
Commissioner Michael Copps
Commissioner Robert McDowell
Commissioner Jonathan Adelstein
Commissioner Deborah Tate

Dear Chairman Martin and Commissioners:

It has come to our attention that a coalition of large telecommunications industry players, including Verizon and AT&T has proposed that the FCC establish a unified $0.0007 terminating access rate for both price cap and rate-of-return carriers. The Rural Telephone Finance Cooperative (RTFC) strongly opposes this proposal. A key lender to the rural telecommunications industry, RTFC currently has over $2.2 billion committed to rural telecommunications companies and cooperatives. Without adequate access revenues, rural telecommunications providers (overwhelmingly rate-of-return carriers) may not be able to repay their existing loans or qualify for new loans.

While RTFC primarily lends to rural telcos for infrastructure modernization and takes a first lien on a borrower's assets, in actuality it is the borrowing telco's level of cash flow that provides us with the truest indicator of its ability to repay the loan. As such, RTFC is very sensitive to potentially significant decreases in key revenue sources.

Access revenues recover a significant portion of a rural local exchange carrier's (RLEC's) costs. According to Professor Dale Lehman's recent study of NECA data on 921 rural local exchange carriers[1], 31% of their regulated revenues came from inter-and intrastate access. If RLECs' terminating access rates are arbitrarily reduced to (a non-cost-based) $0.0007 per minute, rates for other services will have to be significantly increased to make up for the revenue loss. Higher Subscriber Line Charges or local service rates increase the burden on the local ratepayer and increase the likelihood that economically challenged customers who have wireless service will drop their wireline service.

A number of proposals for unifying intercarrier compensation have been proposed and never acted upon in recent years. None were as drastic as what has been proposed by Verizon and AT&T. This plan may work for price cap carriers, but it would be a disaster for RLECs.

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[1] The Next Three Years: Likely Scenarios for Rural Local Exchange Carriers

As an entity extremely familiar with the financial condition of RLECs, RTFC can say unequivocally that the Verizon/AT&T plan for a unified terminating access rate of $0.0007 per minute would end most RLECs' plans for extending increased bandwidth to their customers and negatively impact their ability to repay existing loans. We urge the Commission to reject this proposal and not adopt any intercarrier compensation reform plan that fails to provide for a mechanism to allow RLECs to meet their revenue requirements.

Sincerely,

Lawrence Zawalick
Senior Vice President
Rural Telephone Finance Cooperative

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
High-Cost Universal Service Support and the	)	WC Docket No. 05-337
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
In the Matter of	)	
Developing a Unified Intercarrier Compensation	)	CC Docket No. 01-92
Regime	)	

NTCA

The Voice of Rural Telecommunications
www.ntca.org

INTERIM
UNIVERSAL SERVICE & INTERCARRIER COMPENSATION REFORM PROPOSAL

Respectfully submitted,

Daniel Mitchell
Vice President, Legal & Industry

Its Attorney

4121 Wilson Boulevard, 10th Floor
Arlington, VA 22203
(703) 351-2016

July 11, 2008

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Washington, D.C. 20554

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In the Matter of	)	
Developing a Unified Intercarrier Compensation	)	CC Docket No. 01-92
Regime	)	

NTCA

The Voice of Rural Telecommunications
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INTERIM
UNIVERSAL SERVICE & INTERCARRIER COMPENSATION REFORM PROPOSAL

The National Telecommunications Cooperative Association (NTCA)[1] hereby submits its Interim Universal Service Fund (USF) and Intercarrier Compensation (IC) Reform Proposal ("NTCA Interim USF & IC Reform Proposal" or "NTCA Interim Plan") in response to the Federal Communications Commission ("Commission" or "FCC"), May 2, 2008, News Release encouraging parties to refresh the record in the open dockets addressing universal service reform and/or intercarrier compensation reform.[2]

---

1 NTCA is the premier industry association representing rural telecommunications providers. Established in 1954 by eight rural telephone companies, today NTCA represents 584 rural rate-of-return regulated telecommunications providers. All of NTCA's members are full service rural local exchange carriers (rural LECs) and many of its members provide wireless, cable, Internet, satellite and long distance services to their communities. Each member is a "rural telephone company" as defined in the Communications Act of 1934, as amended (Act). NTCA's members are dedicated to providing competitive modern telecommunications services and ensuring the economic future of their rural communities.

2 See FCC News Release "Interim Cap Clears Path for Comprehensive Reform – Commission Posted to Move Forward on Difficult Decisions Necessary to Promote and Advance Affordable Telecommunications for All Americans." (rel. May 2, 2008) ("FCC News Release").

I. INTRODUCTION

With access revenues shrinking, uncertain universal service reform pending, middle-mile costs increasing, and broadband infrastructure costs soaring, rural service providers and rural consumers are entering a perfect storm. In order to avert this impending danger, the Commission must act quickly to stabilize the federally regulated revenue streams that support rural LEC infrastructure currently used to deploy broadband, as well as provide voice service, to rural consumers living in rural, high-cost areas in the United States. The most expeditious and effective action the Commission can take immediately to avoid this imminent disaster is to cap federal interstate access charges for rate of return carriers at current rates and reassign unrecovered access revenue requirement to the Interstate Common Line Support (ICLS) universal service mechanism. This decisive FCC action now will preserve and advance universal service in high-cost and rural areas, will provide a specific and predictable universal service mechanism,[3] and will allow the Commission to fulfill its statutory responsibility to provide a reasonable cost recovery mechanism for rate of return carriers for the foreseeable future.

II. SUMMARY OF THE NTCA INTERIM USF & IC REFORM PROPOSAL

Contrary to the rhetoric of some, the decrease in access minutes is not simply the evolution away from a "legacy" network. Just as larger companies are migrating their current networks to IP based networks, rate-of-return (ROR) rural companies are also moving to an IP environment. Access charges are simply a "legacy" rate structure adopted and put in place by the Commission as one means of collecting some of the costs associated with the use and provisioning of a network common to both voice and broadband-related services. If access revenue disappears because the rate structure is no longer sustainable - as is now happening at an

3 See requirements in Section 254 (3) and (5).

alarming pace for rural ROR carriers - new rate structures or other means for recovering costs must be established to fund the costs of the common underlying network infrastructure.

Switched access voice services are declining and ultimately cannot be relied on to contribute to the funding for the universal service "social contract" between regulators and communications providers. Nevertheless, some amount of voice access traffic - representing an important part of cost recovery for ROR carriers - will remain in the short-term. But without rate-making intervention such as is proposed herein, ROR carriers' interstate voice access rates will continue to rise as access demand continues its steady, if not accelerating, decline. In today's communications environment access charges have become an unsustainable and flawed regulatory rate mechanism producing ever-rising rates for a service whose use is in permanent decline. The Commission has supported reducing access rates as good regulatory policy. Increasing access rates is contrary to this policy and jeopardizes universal service. That being the case, NTCA proposes that the three steps outlined below be implemented immediately to "plug the holes in the dike" while policymakers deal with more comprehensive long-term USF and IC reform.

NTCA's Interim USF & IC Reform Proposal is directed solely at ROR carriers because the Commission has already resolved interstate access and USF issues for large price-cap carriers through the *CALLS Order*, which capped interstate access rates and created Interstate Access Support (IAS) for price cap carriers.[4] As a result, a decline in switched access usage has no impact on access rates for large carriers. On the other hand, access demand decreases will force

4 Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, CC Docket Nos. 96-262 and 94-1, Sixth Report and Order, Low-Volume Long-Distance Users, CC Docket No. 99-249, Report and Order, Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Eleventh Report and Order, 15 FCC Rcd 12962, (the Commission adopted comprehensive access charge and universal service reform for price cap carriers, based in part on a proposal submitted by the Coalition for Affordable Local and Long Distance Service (CALLS) (*CALLS Order*).

access rate increases for ROR carriers, which in turn hurts ROR carriers, the interexchange carriers that have to pay these increasing charges, and the customers they serve. The ICLS, under NTCA's Interim Plan, will serve the same "relief valve" function for ROR carriers that the IAS now serves for price-cap carriers. NTCA thus proposes the following interim measures for interstate access rate design and residual USF access revenue cost recovery:

1. ROR carriers' federal interstate switched access rates, for NECA pool companies as well as non-NECA ROR companies, should be capped at existing rate levels, until permanent access replacement funding is established for the transition to broadband funding.

2. Access costs that are unrecovered from those capped rates should be recovered from interim USF funding as another component of ICLS, consistent with the existing reliance on ICLS as a residual recovery mechanism for ROR carriers' access-related costs. Even with this additional ICLS support, the overall universal service fund size will likely not increase because of the Commission's recent establishment of a cap on support for competitive eligible telecommunications carriers ("CETCs")[5] and by the future elimination of the identical support rule for CETCs, which will free hundreds of millions of dollars in CETC USF support to be used for this and other purposes.[6] Existing federal high-cost USF mechanisms – High Cost Loop Support, Local Switching Support and Interstate Access Support (for price cap carriers) – and the criteria for existing ICLS support should remain intact through the duration of the interim plan.

3. A proceeding with a specific timeline should be opened to develop a transition from the PSTN universal service system to an IP/broadband universal service system. NTCA recommends that the ultimate IP/broadband USF mechanism for ROR companies should include the characteristics contained in its comments filed earlier this year in the Commission's three universal service Notice of Proposed Rulemakings (NPRMs).[7] Additional, more detailed, recommendations will be forthcoming from NTCA.

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5 See In the Matter of High-Cost Universal Service Support (WC Docket No. 05-337) and In the Matter of Federal-State Joint Board on Universal Service (CC Docket No. 96-45), (rel. May 1, 2008) ("*CETC Cap Order*").

6 See In the Matter of High-Cost Universal Service Support and the Federal-State Joint Board on Universal Service, Notice of Proposed Rulemaking, FCC 08-4, (rel. January 29, 2008) ("Identical Support NPRM")

7 See In the Matter of High-Cost Universal Support. Federal-State Joint Board on Universal Service. WC Docket No. 05-337, CC Docket No. 96-45, Comments filed April 17, 2008, by the National Telecommunications Cooperative Association ("NTCA Comments"). Specifically, the NTCA Comments recommend that the Commission: (1) include broadband in the future definition of universal service; (2) expand the base of USF contributors to include all broadband providers; (3) require all carriers seeking additional or new federal high-cost broadband USF support to submit their Title II regulated costs, revenues and earnings when determining future USF disbursements; and (4) adopt and implement a transition plan to fairly and equitably move the communications industry from the PSTN world to the IP world.

For several years now, access usage and revenues have been declining. As we continue to move inexorably from the Public Switched Telephone Network (PSTN) world to an Internet protocol (IP) based world, both interstate and intrastate access revenues will continue to recede. Soon, the National Exchange Carrier Association (NECA) interstate pool and the NECA settlements that are paid out of the pool will no longer be sustainable. As access usage drops, access rates rise to cover the costs of carriers in the pool. As access rates rise, demand will be further depressed, thus exacerbating the downward spiral in access usage and revenues. The problem will accelerate as consumers adopt IP-based technologies.

The Regulatory Flexibility Act (5 U.S.C. §601) requires the FCC to consider alternative rules that will reduce the economic impact on small entities. NTCA's Interim USF & IC Reform Proposal and NTCA's proposed high-cost universal service reform recommendations filed on April 17, 2008, will reduce the economic impact on small rural providers of the shift to IP-based telecommunications. NTCA's proposals will also allow the Commission to meet its statutory responsibility to provide a reasonable means of cost recovery, will promote the public interest, convenience, and necessity, will spur development of new advanced communications technologies and broadband deployment, and most importantly will ensure that consumers living in rural high-cost areas are able to receive high-quality and affordable voice and broadband services.

III. FEDERAL INTERSTATE SWITCHED ACCESS RATE CAP AND RESIDUAL ICLS REASSIGNMENT

Rate of return carriers derive the revenues necessary to provide service to their customers from several federally established and regulated rate structures and funding mechanisms: (1) subscriber line charges: (2) access charges; (3) universal service funds: (4) cost or average schedule settlements: and (5) other charges to the end user customers. Should any of these rate structures or funding mechanisms shrink appreciably or be eliminated, the funding for rural telecommunications networks will be at risk, endangering those who have come to rely upon these networks — rural consumers and the providers who serve them.

Simply stated, rural ROR carriers face a crisis today precipitated by declining demand for switched access services on the PSTN. Ironically, this reduction in minutes of use on the PSTN has the effect of not only reducing revenues, but also increasing switched access rates for ROR carriers.[8] At some point in near future, the NECA interstate pool and the NECA settlements that are paid out of the pool will no longer be sustainable. As access usage drops, access rates will continue to rise to cover the costs of carriers in the pool. As access rates rise, access demand will be further depressed, thus exacerbating the downward spiral in access usage and revenues. The problem will accelerate as consumers adopt IP-based technologies. More importantly, the reduction in access revenues will directly affect the ability of rural carriers to continue to fulfill current universal service obligations and to invest in broadband infrastructure in rural and high-cost areas of the nation.

As a long-standing policy, and most recently in its *CETC Cap Order* and FCC News Release, the Commission has recognized the interrelationship between any reductions in intercarrier compensation and USF support for rural ROR carriers. For instance, in the news release the Commission stated:

> Universal service support for carriers serving rural, high-cost areas is based on a formula that looks at a carrier's costs and revenues, both from end users and from intercarrier compensation. Many rural carriers currently collect a significant percentage of their revenues from intercarrier compensation in the form of interstate and intrastate access charges. If intercarrier compensation revenues are decreased, demand on the Fund increases as offsetting support payments go up.[9]

8 NECA pool rates are designed to recover the total revenue requirements of ROR carriers. As minutes of use decline more rapidly than the revenue requirement associated with the ROR carriers' networks, the access rates necessary to recover the revenue requirement must increase.

9 FCC News, "FCC Takes Action to Cap High Cost Support Under the Universal Service Fund" (rel. May 1 2008)

The outstanding question that has yet to be answered is: "How to implement further intercarrier compensation reforms while minimizing the impact on USF growth?" NTCA believes that the combination of measures contained in this interim proposal will be a major step toward providing a positive answer to that question, and to setting the stage for further necessary reforms as we move toward the IP world.

In order to stabilize interstate switched access rates, a cap on the aggregate NECA pool interstate switched access rate should be established at the level in effect as of July 1, 2008[10] To recover access costs that would not be recovered due to the cap on access rates, residual revenue requirements would be received from the ICLS so that each carrier would receive a composite revenue total (from interstate access rates and supplemental ICLS) equal to the carrier's total prospective traffic-sensitive revenue requirement. This supplemental support from ICLS would be in addition to each ROR carrier's ongoing ICLS support under existing rules.

Under this proposed cap, rural ROR carriers' switched access rate levels remain cost based, but are limited by a cap. The remaining cost-based access revenue requirement is assigned to ICLS for recovery. In the first year of the plan there would be no residual costs that would need to be recovered through ICLS and it is estimated that at the end of the five years the annual ROR residual costs recovered from ICLS will not be more than $235 million. Three scenarios containing estimated reassignment of access costs from access rates to ICLS for NECA and independent tariff ROR carriers over the next five years under this proposal are shown in Attachment A.[11]

10 For carriers filing their own tariffs, an aggregate federal interstate switched access rate cap should also be established.

11 The Commission could limit the level of residual access costs to be recovered from ICLS by addressing disputes related to the application of access charges. In general, the disputes have involved the following determinations: 1) whether traffic is subject to access charges; 2) which carrier has the financial obligations to pay the access charges;

NTCA's Interim Proposal is directed solely at ROR carriers because the Commission has already resolved these issues for large price-cap carriers. As a result, the decline in access usage has no impact on access rates for large carriers. On the other hand, access demand decreases will force access rate increases for rural ROR carriers, which in turn hurts ROR carriers and the interexchange carriers that have to pay these charges, as well as the customers they both serve. The culprit behind these ever-increasing access rates is the existing access rate structure for rural ROR carriers.

The NTCA Interim Plan directly addresses this problem by capping interstate access for ROR carriers at current levels. The proposal recommends that residual access costs be recovered from ICLS because the Commission initially established the ICLS mechanism to recover residual access costs previously contained in interstate access elements. Allocating additional residual interstate access elements is consistent with the *MAG Order* and, as previously noted, also with the approach the Commission adopted in the *CALLS Order* in establishing IAS. In addition, allowing recovery of both traffic-sensitive and non-traffic-sensitive costs from ICLS is also consistent with the *MAG Order*.[12] Recently, the Commission allowed certain carriers who converted from ROR to Price Cap regulation to retain their ICLS.[13]

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and 3) which carrier has the responsibility to make available the proper and necessary information in order to assess and bill access charges on access traffic. First, the Commission should grant the NECA Petition thereby extending call signaling rules to all carriers and interconnected voice service providers, including IP-enabled providers (as would the Signaling Act), and clarifying the application of these rules. Along with these actions, the Commission should also resolve the long-standing Arizona Dialtone Petition request by specifying the correct number to pass in the CN parameter to facilitate correct billing treatment for the call. Next, the Commission should grant the Embarq Petition related to the ESP exemption on any IP-to-PSTN voice traffic. Finally, the Commission should adopt a portion of the interim phantom traffic proposal filed by Missoula Plan Supporters, calling for the creation and exchange of call detail records and call summary information.

12 See In the Matter of Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers, Second Order and Further Notice of Proposed Rulemaking, FCC Docket No. 01-304, (rel. October 11, 2001) ("*MAG Order*"), ¶¶ 100 & 136, ftn. 375.

13 The Commission has also found that it is appropriate for carriers that were rate-of-return that convert to price cap regulation to continue to receive high-cost universal service support to explicitly recover their common line costs by

To effectuate this proposal, each ROR carrier, filing independently or through NECA, will be required to file its prospective traffic-sensitive revenue requirements[14] and prospective interstate switched access demand for the test year with the Commission. Based upon these filings, the Universal Service Administrative Corporation ("USAC") would then make the appropriate adjustment to the company's ICLS distribution based on the difference between the estimated revenue from switched access rates in the test period and the total estimated (unadjusted) switched access revenue requirement. To maintain the alignment between cost and rates, all NECA and independent tariff ROR carriers will develop an adjustment factor for each test year which, when applied to the traffic sensitive (TS) revenue requirement, will determine which costs are subject to interstate access ratemaking and which costs will be attributable to ICLS recovery. This supplemental ICLS recovery would be subject to subsequent true-up, just as ICLS is today.[15]

Again, this important change in the ratemaking process for interstate switched access is consistent with the policy that the Commission first applied in its last significant reform of intercarrier compensation for ROR carriers in 2001 when ICLS was established.[16] In the *MAG Order*, the Commission shifted ROR carriers' costs from various interstate access elements to be recovered from a new, explicit USF support mechanism, ICLS. In its deliberation in the *MAG Order*, the Commission changed the cost recovery for line ports and the transport interconnection charge (TIC) from switched access rates to ICLS.

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allowing such carriers to continue to receive ICLS. *See Windstream Petition for Conversion to Price Cap Regulation and for Limited Waiver Relief*, WC Docket No. 07-171, Order (rel. Mar. 18, 2008), ¶¶ 19-22.

14 For those companies electing average schedule treatment, estimated average schedule settlements would be a proxy for those companies' costs, as is done today within the pool.

15 See 47 C.F.R. §54.903(a)(4).

16 See *MAG Order*, ¶¶ 100 & 136, ftn. 375.

The Commission adopted a proxy of 30 percent as the portion of overall local switching costs associated with line ports, and thus allocated that amount to the common line category.[17] In the *MAG Order*, the Commission recognized that ROR carriers' line port costs may vary widely, and also indicated an awareness that some carriers' line port costs were significantly more than 30 percent of total local switching costs.

In similar fashion, the Commission concluded that TIC costs were related to different access categories and represented both traffic-sensitive costs and non-traffic-sensitive costs. Thus, it ordered that the TIC costs were to be spread proportionately to all other rate elements.[18] While it stated that equally valid alternative methods for assigning TIC costs could have been adopted, the Commission admitted that it could not determine from the record in the proceeding the exact portion of the costs recovered from TIC that were transport related.[19]

For both local switching costs and TIC-related transport costs, it would be entirely consistent with the Commission's action in the *MAG Order* to assign a different proportion of local switching and transport cost between the common line, switching and transport categories and to recover these common line costs with a supplemental distribution from ICLS as proposed in this plan. The ICLS mechanism developed by the Commission can accommodate additional costs that may be re-categorized as common line costs upon further reconsideration. In initially establishing the ICLS without a cap, the Commission recognized that allowing recovery of interstate access costs is essential for ROR carriers because those companies are "particularly sensitive to disruptions in their interstate revenue streams."[20]

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17 See *MAG Order*, ¶94.

18 See *MAG Order*, ¶100.

19 See *MAG Order*, ¶101.

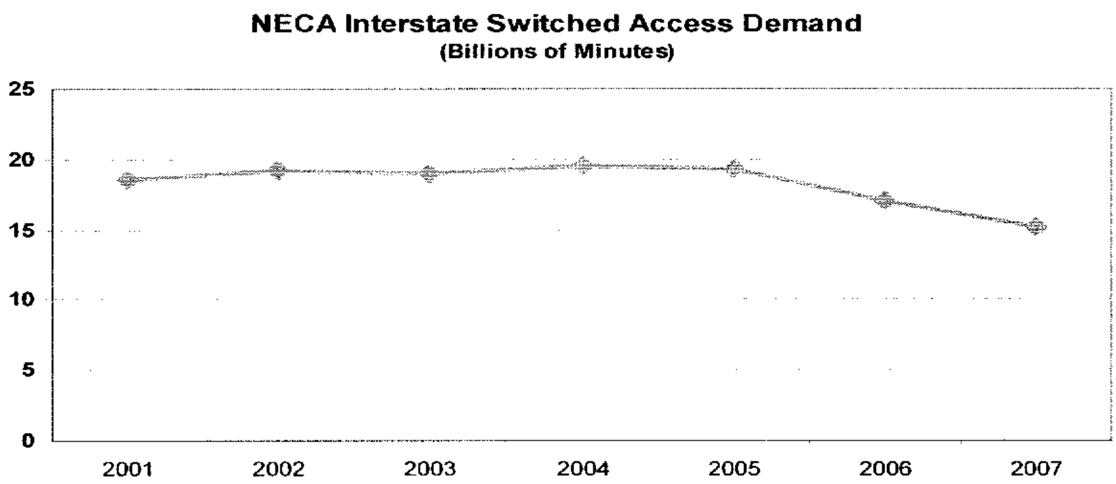
20 See *MAG Order*, ¶ 134.

The capping of interstate access rates and reassigning of access-related costs to ICLS is necessary to remedy the looming disruption of ROR carriers' operations and universal service obligations to their customers. The precipitous decline in switched access traffic constitutes a serious, ultimately debilitating effect on ROR carriers' ability to serve their customers, thus requiring immediate action. In its 2008 interstate access tariff filing, NECA forecasted local switching minutes to decline by almost 12 percent.[21] This forecasted decrease was on top of an 11.4 percent reduction from 2006 to 2007 that NECA had previously reported.[22] Given the shift away from long-distance service to other services that do not utilize switched access, it is obvious that ROR carriers' switched access demand will continue to decline. This reduction in interstate access demand will result in ever escalating access rates for ROR carriers unless this Commission takes immediate interim action. The current and forecasted decline in switched access demand and the resulting and forecasted increase in switched access rates are clearly

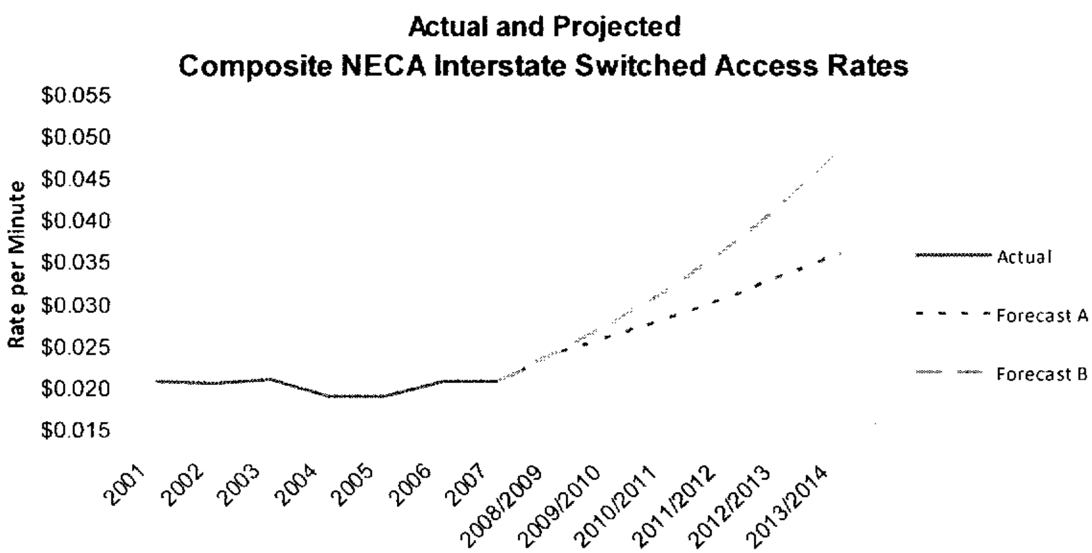
21 See NECA Access Service Tariff F.C.C. No. 5, Transmittal No. 1214, June 16, 2008, Volume 3 at p. 4. This decline is measured by comparing the forecast for the 2008/2009 tariff period against the actual minutes of use for the 2007 calendar year.

22 See NECA TRP filing Excel File; sheet 'DMD-1 Page 3'. Percent decline represents the change from actual 2006 minutes of use to actual 2007 minutes of use.

shown in the graphs below.[23]



Source: Tariff Review Plans



Source: Tariff Review Plans and Consortia Consulting Forecast
Forecast C was omitted as the forecast resulted in a line overlapping Forecast B.

23 The forecast of switched access rates assumes that pool composition remains constant, i.e., no pool members enter or exit the pool, and that revenue requirements do not shift between switched and special access.

Implementing a cap on interstate rates will ensure that ROR carriers' access rates do not continue to increase, which will benefit multiple parties. Interexchange carriers will benefit by paying lower access rates than they otherwise would if rates were not capped. Since interexchange carriers pass on access costs in their retail long-distance rates, customers will also benefit by paying lower retail long-distance rates. Moreover, rural customers will also continue to receive the high-quality service and will benefit by rural carriers' continued investment in broadband infrastructure.

In addition, implementing the recovery of residual common line revenue requirements from ICLS for ROR is also sound public policy, building on the record in the *MAG Order*. Since supplemental support it is limited solely to ROR carriers, which represent a small portion of the nation's access lines relative to price cap carriers, such a change will not result in large increases in the USF.[24] Indeed, recently in its *CETC Cap Order*, the Commission observed that both Local Switching Support and ICLS for ROR carriers have been stable in recent years.[25] Thus, the stability in the size of ICLS for incumbent LECs that the Commission anticipated seven years ago in the *MAG Order* has occurred. This stability should continue under NTCA Interim USF & IC Reform Proposal

Immediately following the Commission's issuance of an order adopting this proposal, NTCA recommends that the Commission issue a notice of proposed rulemaking to institute the plan within 90 days. The interim plan may expire after the full implementation and completion of the FCC's more comprehensive long-term high-cost USF and IC reforms, unless the Commission then determines that it is appropriate to continue the cap and supplemental ICLS

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24 In the *MAG Order*, the Commission also observed that ICLS will be constrained by carriers' embedded costs and recalculated annually to recoup any unrecovered costs. See *MAG Order*, ¶¶ 133-134.

25 See *CETC Cap Order*, ¶ 10.

based on the lifecycle of switched access or other reasons. By that time, however, it is reasonable to project that the contribution of switched access to ROR carriers' incomes will have decreased to such an extent so as to be negligible and market conditions will likely warrant implementation of an IP universal service system.

IV. COMMISSION SHOULD INITIATE A PROCEEDING TO INVESTIGATE THE IMPLICATIONS OF THE IP PARADIGM SHIFT ON UNIVERSAL SERVICE AND BROADBAND DEPLOYMENT.

The models for exchange of Internet traffic are drastically different from models for exchange of PSTN traffic.[26] The financial responsibility for the exchange of PSTN traffic is borne by either the "owner" of the retail relationship (as is the case for access traffic) or the originator of the call (as is the case for reciprocal compensation traffic). For the exchange of Internet traffic, the financial responsibility lies with the entity with the lesser comparable value in the traffic exchange. Thus, as applications converge to IP network platforms, intercarrier compensation dollars flow from the smaller providers to the larger providers.

This compensation scenario presents a major problem for small network service providers, such as the ROR carriers serving the most rural areas of the country. Instead of being recipients of intercarrier compensation revenue (through access charges and reciprocal compensation), the IP revenue flows are reversed, and small, rural ROR carriers become payers. Without traditional intercarrier compensation revenue, rural ROR carriers cannot fund advanced network investment. In other words, the shift of traffic to IP threatens the ability of small carriers to continue providing access to that same IP-based world.

The Commission must recognize that this fundamental shift in compensation threatens the ability of rural carriers to build the necessary infrastructure to provide quality advanced and

26 Although, as has been observed, there is widespread existence of IP-enabled traffic that utilizes the PSTN, and in such instances it is becoming increasingly apparent that sound policy calls for payment by IP providers when they utilize PSTN resources.

information services at just, reasonable and affordable rates. This fundamental shift in compensation is the reason that NTCA proposes as part of this interim plan that the Commission initiate a proceeding to investigate the implications of the IP paradigm shift on universal service and ability of rural carriers to deploy broadband.

In its recent filing with the Commission on the three USF NPRMs, NTCA made several recommendations related to long-term high cost universal service reform.[27] NTCA believes that its recommendations provide the basis for a further investigation and proposed rulemaking by the Commission.

NTCA proposed that as an initial action, broadband service should be included in the definition of universal service.[28] The Commission should include, in the proposed new proceeding, an investigation into the specific nature of the broadband service that would be included in the definition of universal service. The Commission should also investigate the legal foundation for including generally available broadband services.

Second, based on NTCA's recommendation, the Commission should offer for comment a tentative conclusion that USF contribution responsibilities be expanded to include all broadband service providers, [29] which would include providers of both public and private broadband service. These providers all have a telecommunications component in the delivery of their services offered for a fee. Because of this, the Commission has a solid legal framework for expansion of the USF contribution base to include broadband service providers.

Finally, as proposed by NTCA, the Commission should investigate the costs associated with middle-mile and Internet backbone services for small ISPs providing service in rural areas

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27 See NTCA Comments filed on April 17, 2008 in WC Docket No. 05-337 and CC Docket No. 96-45.

28 *Id.*, p. 8.

29 *Id.*, p. 9.

and consider implications for access to advanced information services.[30] In many rural areas, consumers have only one quality alternative for broadband Internet access and that is the rural LEC's affiliated ISP. As applications migrate to IP platforms, the affiliated ISP becomes the Internet lifeline for many rural consumers. Without major reforms, however, these rural consumers are at risk of not having this lifeline.

NECA performed an extensive analysis of middle-mile costs in a recent study.[31] NECA's findings were dire—concluding that high-speed Internet service is uneconomic in many rural areas. NECA further found that increased IP traffic will exacerbate, rather than ameliorate, the problem, as existing revenue shortfalls are multiplied as the scale of operations increases. For example, the study shows revenue shortfalls at $9.7 million per year at a 0.5% penetration rate, growing to $33.6 million per year at a 5% penetration rate, $49.8 million at a 10% penetration rate, and $63.8 million per year at a 15% penetration rate.[32] NECA's sobering conclusion: "high-speed Internet service may not be sustainable in many rural areas based on pure economics."[33]

NTCA members report similar realities. While the cost of purchasing Internet capacity on a per-megabit basis has gone down over the last several years, large increases in customer demand require small rural LECs to buy more and more broadband/Internet capacity, thus middle-mile cost have increased dramatically. One NTCA member company, which provided NTCA with cost data under the proviso that its identity not be revealed, reported that total bandwidth costs for backhaul purposes increased by 105% between 2001 and 2008. Over the

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30 *Id.*, pp. 49-50.

31 National Exchange Carrier Association (NECA), Middle Mile Broadband Cost Study, October 2001.

32 NECA, Middle Mile Cost Study Executive Summary, www.neca.org/source/NECA_Publications_1154.asp.

33 *Ibid.*

same period, Internet access capacity costs increased by more than 500%. While these cost increases were, in part, offset by increased broadband revenues, the average cost per customer is increasing because consumers are consuming increasingly larger quantities of bandwidth. At the same time carriers have limited ability to raise rates due to affordability constraints.

Risk and reward are the principal factors in determining both the availability and the cost of investment capital. Financing from Rural Utilities Service, CoBank, Rural Telephone Finance Cooperative and other sources will dry up for small rural broadband providers if the investments become too risky because of lost access revenues, and increased broadband-related costs. Absent Commission action, current loans could be at risk since revenues are falling and the broadband infrastructure that has been deployed has not yet been paid for. Consequently, it will become increasingly difficult, if not altogether impossible, for rural ROR providers to continue to deploy, upgrade and maintain their broadband infrastructure. Broadband deployment in rural areas served by ROR carriers will be slowed or stop dead in its tracks. Pushed to the extreme, it is possible that a financial crisis could develop for rural ROR carriers, just as is happening today in the mortgage banking industry.

This broadband cost trend is obviously not sustainable, and it threatens the ability of rural ROR carriers to continue providing broadband services to their customers. The Commission should initiate an investigation into the costs charged to small carriers and rural ISPs associated with middle-mile and Internet backbone services to preserve access to advanced information services in rural areas.

V. THE ROLE OF THE STATES IN USF AND THE IMPLICATIONS OF SEPARATIONS REFORM IN AN IP/BROADBAND WORLD

Today, the method for the allocation of accounting costs and revenue between the states and the federal jurisdiction consists of an elaborate combination of allocations, direct assignments, and actual use measurements.[34] Essential to the current separations process is the application of a Uniform System of Accounts and the ability to measure traffic between defined end points in a circuit-switched environment, where the locations of the end points of a call determine the jurisdiction of the traffic and, therefore, the allocation of certain network costs to a jurisdiction. Allocated costs and jurisdictional traffic demand are used in the interstate jurisdiction (as well as in many states) to provide the basis for access charge ratemaking.

In such jurisdictions, the allocation of costs and revenues is also the foundation for the assessment and distribution processes in universal service funding systems. The federal rules allocate a portion of loop cost to the federal jurisdiction if loop costs in a study area are extraordinary.[35] For rural carriers, these extraordinary loop costs reassigned to the federal jurisdiction are recovered through the federal High Cost Loop Support program. A similar process applies to switching cost and recovery through the federal Local Switching Support program.[36]

Significant questions arise if one attempts to apply the current separations process to the IP world. First, if accounting costs associated with the production of IP services are to be assigned to jurisdictions, one must apply a uniform accounting system to the IP world. Further, the allocation of costs based on actual use requires that the end points of a transmission be determined. What parameter would be used to measure actual use, and for what service or services would such usage would be measured is yet unknown.[37] Finally, even if allocation principles can be identified (based on actual use or some other measure), the means by which

34 47 C.F.R. § 36.2 (a)

35 47 C.F.R. § 36.631 Expense Adjustment

36 47 C.F.R. § 54.301 Local Switching Support

37 It is also perhaps nonsensical to measure both connection-oriented and connectionless transmissions on an IP-based network.

states would collect monies in order to fund broadband costs allocated to their jurisdiction is also undetermined.

As part of establishing a new USF regime in the IP/broadband environment, NTCA further recommends that the Commission drastically modify existing separations rules. As such, a determination should be made in this IP/broadband rulemaking as to the portion of ROR carriers' costs that are to be funded by the states. Although it is difficult to determine the nature of IP traffic and the Commission historically has categorized these new services as interstate, NTCA believes it is necessary and appropriate that states have some role in meeting a portion of the funding obligation. That being the case, another critical part of the USF proceeding proposed in the NTCA plan would be an inquiry into the issues of separations, the states' roles for the recovery of a portion of IP-related network costs, and the portion of IP-related network costs that should be allocated to the state jurisdiction.

VI. THE FCC HAS A STATUTORY RESPONSIBILITY TO ADOPT A RATE STRUCTURE OR MECHANISM THAT PROVIDES AN OPPORTUNITY FOR ROR CARRIERS TO RECOVER COSTS INCLUDING A REASONABLE RETURN AND DOES NOT RESULT IN A CONFISCATORY TAKING

The Commission has an obligation to address serious flaws with the current Commission-established access rate structure. In so doing, the Commission will sustain universal service and provide incentives for continued rural broadband investment. Utilities are protected from the taking of their property by the United States Constitution. This protection extends to a prohibition on the setting of confiscatory rates that result in a taking of property.

Pursuant to the 5th Amendment,[38] Sections 201 and 254 of the Act, and existing regulatory precedent,[39] the Commission has a legal responsibility to provide rates and a rate

38 United States Constitution, Amendment V.

structure for rural ROR carriers that does not result in a confiscatory taking and will provide an opportunity to recover costs as well as earn a reasonable return on those investments made to provide service.[40] The Commission has previously recognized this responsibility, specifically stating that "[r]ate-of-return carriers charge rates that are designed to provide the revenue required to cover costs and to achieve a prescribed return on investment."[41] In exchange for a reasonable opportunity to recover costs including a reasonable return, ROR carriers have provided quality service at rates reasonably comparable to those in urban areas to **all** rural consumers in the areas they serve, and have fulfilled all carrier of last resort obligations.

Courts have long evaluated utility rates against the back drop of the requirements of the Constitution and confiscatory rates. i.e., *Bluefield Water Works v. Public Service Commission* 262 U.S. 679 (1923) and *Federal Power Commission, et al. v. Hope Natural Gas Co., et al.*, 320 U.S. 591 (1944). It is clear that "[t]he Constitution protects utilities from being limited to a charge for their property serving the public which is so 'unjust' as to be confiscatory." *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 307-308 (1989) (citing *Covington & L Turnpike Road Co. v. Sandford*, 164 U.S. 578, 597 (1896) (A rate is too low if it is "so unjust as to destroy the value of [the] property for all the purposes for which it was acquired," and in so doing "practically deprive[s] the owner of property without due process of law"); *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U.S. 575, 585 (1942) (summary omitted.); *Federal Power Commission v. Texaco, Inc.*, 417 U.S. 380, 391-92 (1974)) (summary omitted.)

39 See In the Matter of Federal State Joint Board on Universal Service, CC Docket No. 96-45, FCC 01-157, Fourteenth Report & Order (May 23, 2001) ("*RTF Order*"), ¶¶ 24 and 25. See also, *MAG Order*, ¶¶ 3, 12, 131, 132, and 134.

40 See *F.C.C. v. Florida Power Corp.* 480 U.S. 245, 253-254 (1987).

41 *MAG Order* (FCC 01-304), ¶19.

To guard against a confiscatory rate, the Commission should employ the general standard that the rate mechanisms used by the Commission should provide a ROR carrier with a reasonable opportunity to recover costs, including a reasonable rate of return.[42] This standard does not guarantee a return, but requires the opportunity. The current situation does not provide this opportunity.

The access situation is deteriorating. The Commission has no choice but to act on this matter because a failure by the Commission to act will ultimately result in confiscatory rate mechanism for ROR carriers. Consequently, inaction is not an option and will only spawn Constitutional taking claims by ROR carriers. This result is unnecessary and as in the past we expect that the Commission will recognize that "rate-of-return carriers are particularly sensitive to disruptions in their interstate revenue streams"[43] and take action to address the problem. The plan provided in this filing sets forth a reasonable approach to resolve this issue on an interim basis and to fulfill the Commission's statutory obligations.

The Commission has consistently recognized this legal responsibility and has regulated in a manner that allows ROR carriers to recover their costs along with a reasonable return on investment.[44] The Commission has also recognized the unique characteristics of rural ROR carriers and the unique challenges they face in providing quality service to their customers.[45]

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42 See, discussion of *Federal Power Commission v. Hope Natural Gas*, 320 U.S. 591 (1944) in Duquesne at 310. "Today we reaffirm these teachings of Hope Natural Gas: "[I]t is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unreasonable, judicial inquiry ... is at an end. The fact that the method employed to reach that result may contain infirmities is not then important." Id., at 602, 64 S.Ct., at 288. This language, of course, does not dispense with all of the constitutional difficulties when a utility raises a claim that the rate which it is permitted to charge is so low as to be confiscatory: whether a particular rate is "unjust" or "unreasonable" will depend to some extent on what is a fair rate of return given the risks under a particular rate-setting system, and on the amount of capital upon which the investors are entitled to earn that return. At the margins, these questions have constitutional overtones."

43 *MAG Order*, ¶ 134.

44 *RTF Order*, ¶¶ 24 and 25 and *MAG Order*, ¶¶ 3, 12, 131, 132, and 134.

45 *RTF Order*, ¶¶ 24, 25, and 79 and *MAG Order*, ¶¶ 3, 12, 131, 132, and 134.

The Commission articulated the unique characteristics of rural ROR carriers, their dependence on access charge revenues, and the need to preserve universal service in the *MAG Order*, stating that "Our examination of the record reveals that rate-of-return carriers generally are more dependent on their interstate access charge revenue streams and universal service support than price cap carriers and, therefore, more sensitive to disruption of those streams. . . . . The approach that we adopt will provide these carriers with certainty and stability by ensuring that the access charge reforms we adopt do not affect this important revenue stream."[46] The Commission and the Joint Board have recognized that ROR regulation along with the universal service fund have worked well in rural areas, not only for providing quality service at reasonable rates but also for deploying broadband in rural areas.[47] Now is the time for the Commission to take the next step to address the current access rate structure problem.

VII. CONCLUSION

The Commission has a legal responsibility to provide ROR carriers with an opportunity to recover costs as well as to earn a reasonable return on those investments. In exchange for a reasonable opportunity to recover costs including a reasonable return, ROR carriers have provided quality service at rates reasonably comparable to those in urban areas to **all** rural consumers in the areas they serve. The current access charge system can no longer provide a reasonable opportunity to recover costs and therefore the Commission must take immediate action if it is to fulfill its legal responsibilities.

Failure to act will result in little or no additional investment in broadband infrastructure and will result in a painful, potentially devastating crisis for rural telecommunications customers and the carriers that serve them. If such a scenario were allowed to transpire, rural customers

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46 *MAG Order*, ¶ 131.

47 *MAG Order*, ¶ 224 and Joint Board Recommended Decision, ¶¶ 30 and 39.

served by ROR carriers would likely have few, if any, others means for receiving telecommunications services because the rural ROR carriers provide the underlying networks necessary for other technologies, such as wireless, to operate. In a very real sense, these rural customers will be disconnected from the emerging IP-based economy. Failure to act will also mean that the Commission has failed to fulfill its statutory obligations. NTCA urges the Commission to implement NTCA's Interim USF & IC Reform Proposal now in order to fulfill its legal responsibility to provide a reasonable cost recovery mechanism, to preserve and advance universal service in high-cost and rural areas, and to provide a specific and predictable universal service mechanism.

The Regulatory Flexibility Act (5 U.S.C. §601) requires the FCC to consider alternative rules that will reduce the economic impact on small entities. NTCA's interim and long-term USF and IC reform recommendations would reduce the economic impact on small rural broadband providers and rural consumers. NTCA's proposals will allow the Commission to meets its regulatory responsibility, will promote the public interest, convenience, and necessity, will spur development of new advanced communications technologies and broadband deployment, and most importantly will ensure that consumers living in rural high-cost areas are able to receive high-quality, affordable voice and broadband services. NTCA therefore urges the Commission to adopt NTCA's recommendations and ensure consumers living in rural high-cost areas are able to receive high-quality, affordable voice and broadband services.

Respectfully submitted,

NTCA

NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION

The Voice of Rural Telecommunications
www.ntca.org

By: /s/Daniel Mitchell
Daniel Mitchell
Vice President, Legal & Industry

Its Attorney

4121 Wilson Boulevard, 10th Floor
Arlington, VA 22203
(703) 351-2016

CERTIFICATE OF SERVICE

I, Adrienne L. Rolls, certify that a copy of the National Telecommunications Cooperative Association's (NTCA's) Interim Universal Service Fund (USF) and Intercarrier Compensation (IC) Reform Proposal in WC Docket No. 05-337, CC Docket No. 96-45 and Docket No. CC 01-92 in response to the FCC, May 2, 2008 News Release was served on this 11th day of July 2008 by first-class, United States mail, postage prepaid, or via electronic mail to the following persons:

Chairman Kevin J. Martin
Federal Communications Commission
445 12th Street, SW, Room 8-B201
Washington, D.C. 20554
Kevin.Martin@fcc.gov

Commissioner Deborah Taylor Tate
Federal Communications Commission
445 12th Street, SW, Room 8-A204
Washington, D.C. 20554
Deborah.Tate@fcc.gov

Commissioner Michael J. Copps
Federal Communications Commission
445 12th Street, SW, Room 8-B115
Washington, D.C. 20554
Michael.Copps@fcc.gov

Commissioner Jonathan S. Adelstein
Federal Communications Commission
445 12th Street, SW, Room 8-A302
Washington, D.C. 20554
Jonathan.Adelstein@fcc.gov

Commissioner Robert M. McDowell
Federal Communications Commission
445 12th Street, SW, Room 8-C302
Washington, D.C. 20554
Robert.McDowell@fcc.gov

Best Copy and Printing, Inc.
Federal Communications Commission
445 12th Street, SW, Room CY-B402
Washington, D.C. 20554
fcc@bcpiweb.com

/s/ Adrienne Rolls
Adrienne Rolls